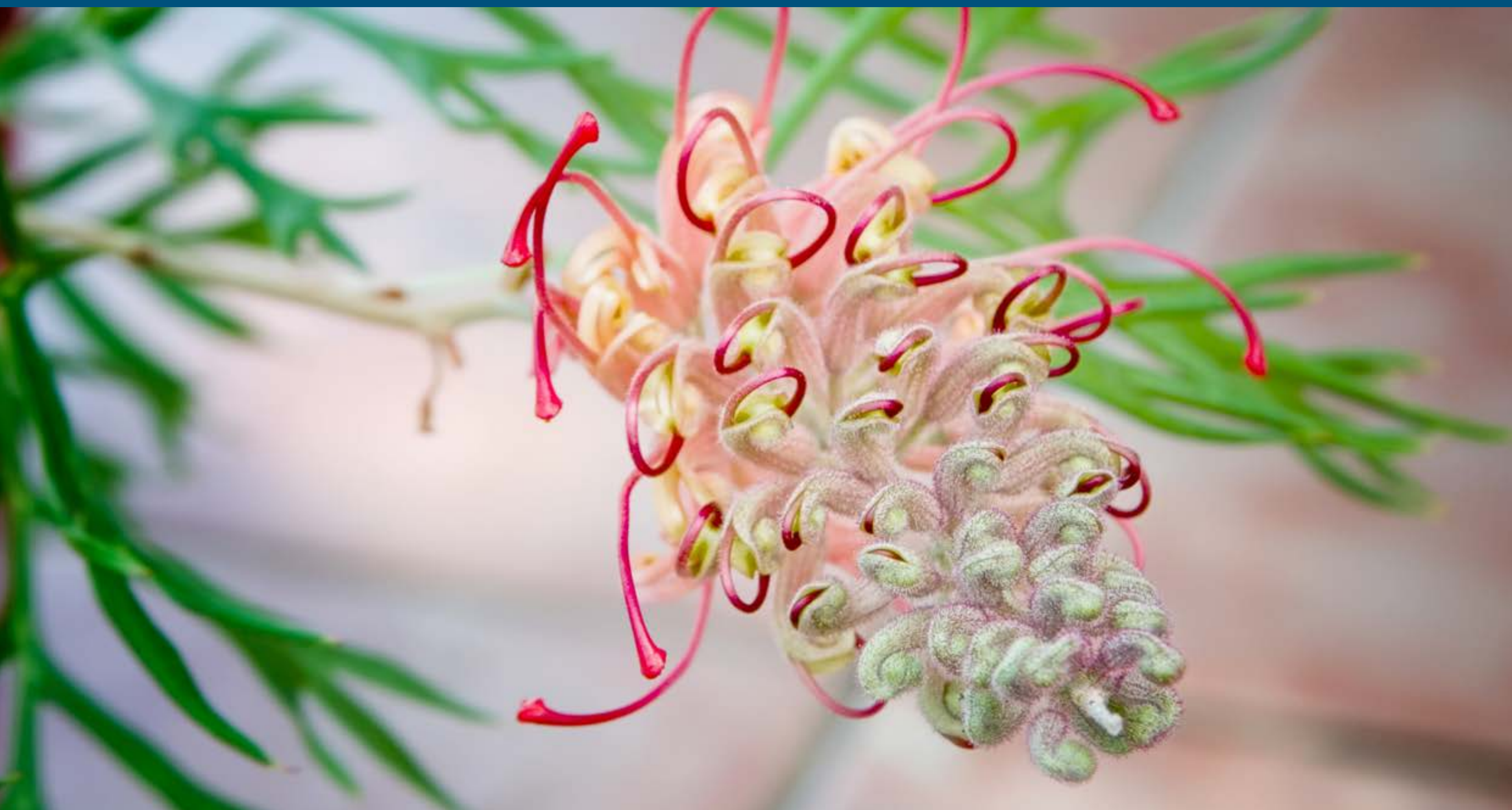
HERBERT SMITH FREEHILLS

THE PANEL IN A NED KELLY COUNTRY

20 YEARS OF THE AUSTRALIAN TAKEOVERS PANEL



In his June 1972 article in the *Australian Law Journal*, Kim Santow mused that Australia should have an equivalent of the London Panel on Takeovers and Mergers – albeit with the recognition that penal sanctions would likely be required 'in a Ned Kelly country still lacking a developed 'City''

Front cover: *Grevillea bipinnatifida x banksii* – 'the Ned Kelly Grevillea'

Introduction

The creation of an Australian Takeovers Panel was not a new idea. For decades, the late Hon Justice Kim Santow AO, former M&A partner of Freehill, Hollingdale & Page, Judge of the NSW Supreme Court and Judge of the NSW Court of Appeal, argued for the creation of an Australian takeovers panel.

In his June 1972 article in the *Australian Law Journal*, Kim Santow mused that Australia should have an equivalent of the London Panel on Takeovers and Mergers, albeit with the recognition that penal sanctions would likely be required 'in a Ned Kelly country still lacking a developed 'City'. '

In referring to the London Panel, Kim noted:

> 'One might hope that Australia could achieve a similar self governing system with all its advantages. The disuniform legislation we now have is frequently cumbersome and obscure and inappropriate to govern business ethical standards, as distinct from the basic legal requirements.'

Kim continued to be a powerful advocate for a takeovers panel and served as one of its earliest members. Kim was well ahead of his time, in both the idea for a panel but also for identifying that more broadly, ethics and business were going to be an important theme going forward.

On the 20th anniversary of the modern Takeovers Panel, we hope you enjoy reading *The Panel in a Ned Kelly Country*.















Contents

Rodd Levy

Cheers to 20 years of the Takeovers Panel

It took a long time for the Panel as we know it to come to be. London established its Panel as far back as 1968. Despite some early scepticism, it was soon regarded as a success. So much so that in 1972 the late, great, Kim Santow was urging Australia to follow suit.[1] After experimenting in the 80s with giving the NCSC the power to declare acquisitions unacceptable based on policy objectives, then creating the barely used forerunner to the Panel in the early 90s and taking stock under the CLERP program, the Panel as we know it was eventually established in March 2000.

Over the last 20 years, the Panel has proven to be a great success. It has dealt with countless disputes and provided market guidance on a range of crucial issues. It has vastly improved Australia's market for corporate control. As a sign of how well designed the model was, the Panel survived a High Court challenge to its legitimacy unscathed and there have been very few changes in the structure or operation of the Panel since 2000. It is the predominant policy setter and takeover dispute resolution body in our market. Even when parties are able to litigate their disputes in the courts, resorting to litigation in this context is extremely unusual. The Panel has achieved the goal, as articulated by Kim Santow in Pinnacle VRB Ltd, of being not a second rate court, but a 'first rate commercial panel'

I intend to highlight five pivotal developments in the last 20 years of the Panel. Each illustrates how the Panel has approached its work and has improved Australia's market for corporate control.

Break fees

This is a prime example of the Panel's ability to resolve an uncertainty in the market without waiting for the Government to intervene with a legislative response.

Break fees started to emerge in the Australian market in the late 90s, following US practice. In the early days, these were highly controversial. The chairman of a very prominent Australian company told me that he would 'never' agree to a break fee as he 'didn't believe in them'. In his view, shared by many in the market at the time, break fees unfairly allocated the risk of a transaction not proceeding. In those days, there was uncertainty about whether a break fee was lawful and whether the amount needed to be capped.

The Panel deftly resolved the uncertainty in 2001 by devising a rule of thumb that a break fee of up to 1% of the equity value of the target company would be regarded as acceptable.

The '1% rule', which was the same percentage adopted in the London market, though much less than the common US practice, has been followed ever since and is considered as the appropriate amount for most transactions. It has been cited frequently by the courts in assessing the reasonableness of break fees in transactions that have come before them (mainly in the context of schemes of arrangement).

Frustrating action policy

This policy evolved to deal with the issue of what should happen if a board takes action which prevents a bid being considered on its merits, such as issuing new shares after a bid is announced. The courts' test historically was simply to ask whether the directors took the action in discharge of their duties to promote the best interests of the company as a whole. If they did, then the courts would not set the action aside, even if it had the effect of frustrating a current takeover bid.

When the takeovers legislation was amended in 2000, the ability for the Panel to declare circumstances to be unacceptable was expressly extended so that it might apply to actions taken by the target company. Previously, it was accepted that the Panel's powers could only apply to action taken by a bidder.

This approach was tested in Reliable's takeover bid for Pinnacle VRB Ltd in 2001. The bid included a condition that there be no material transactions outside the ordinary course of the business. A few months into the bid, the target announced that, to further the prospects of the company, it would grant a licence to market the

1. Some aspects of regulating takeovers and mergers in Australia (1972) 46 ALJ 269. Kim Santow was a partner at Freehill, Hollingdale and Page from 1965 to 1993 and subsequently a judge of the NSW Supreme Court and Chancellor of the University of Sydney.

company's technology in the Americas to a 22% shareholder. The bidder applied to the Panel seeking orders setting aside the transaction.

In the well-known decision, the Panel, led by Justice Santow (as he then was) sitting as a member of the Panel, declared that the transaction was unacceptable as it had frustrated the bid. This matter did not turn on questions of directors' duties or proper purpose. The Panel's view was that matters regarding the control of a company should be decided by shareholders, not by the board of directors. The Panel set aside the transaction unless target shareholders, on a fully informed basis, were to approve the transaction.

This was a major change in approach, as evidenced by the extent of the commentary about the decision that appeared in various journals at the time.

The development of the frustrating action policy is one of the key achievements of the Panel. Through various refinements of the relevant guidance note which now articulates the policy, the Panel has established a workable set of rules that preserves the primacy of shareholders' interests to receive the takeover bid, while balancing the need for a company to carry on its normal business.

Equity derivatives

Equity derivatives first came to prominence in an Australian takeover scenario in 1996 when Brierley Investments Ltd used equity swaps to enable it to purchase up to 25% of the shares in John Fairfax Holdings Ltd without being exposed to share price fluctuations. At the time, equity derivatives were increasingly being used in markets around the world and regulators were endeavouring to work out whether they were legal, whether their use should be permitted and how to deal with the thorny question of when and what disclosure was required. There were calls for the Australian Government to introduce laws for disclosure requirements to cover derivatives. Despite those calls, no legislation was introduced.

Matters came to a head in Centennial Coal's bid for Austral Coal in 2005. Glencore had secretly built a 12% stake in the target, comprising just under 5% held in shares and the balance via equity derivatives. The stake only became public after the bid was declared unconditional and the bidder held acceptances for more than 30% of issued shares. Once it became clear that the shares held by the swap counterparties would not be accepted into the bid, Centennial applied to the Panel arguing that the non-disclosure meant that the market for Austral shares was not efficient, competitive or informed.

There was a long saga before the Panel with various arguments being raised about the use and nature of the derivatives. Ultimately, the Panel rejected the argument that Glencore had a 'relevant interest' in the underlying shares due to the arrangements with the investment banks, but it nevertheless concluded that the non-disclosure had created unacceptable circumstances.

The Panel subsequently issued guidance providing that, in control situations, the Panel expects holders of derivatives relating to more than 5% of voting shares to disclose their interests. At the time, the Federal Government was expected to soon legislate its own disclosure regime. With that in mind, the Panel limited its guidance to apply only in situations where a control transaction was on foot.

Fifteen years later, no legislation has emerged. However, as a sign of leadership on the issue, the Panel in 2019 proposed a revised guidance note stating that it expected all positions over 5% whether held through derivative or through physical shares, to be disclosed, irrespective of whether there is a control transaction on foot or not.

Truth in takeovers

One of the key objectives of the takeovers legislation is to ensure market integrity. This has translated into a view that a market participant who makes a statement as to what they will do in the course of a takeover should be held to that statement. This is known as the 'truth in takeovers' principle.

The policy came about after instances in the 90s where bidders, seeking to encourage shareholders to accept the bid on the table, would state that they had no intention of increasing the offer price, only to change their mind later. The subsequent increase not only disappointed accepting shareholders, but also anyone who had sold on market.

The issue came to the Panel's attention in two of the largest takeovers in Australian corporate history.

Rodd Levy
Cheers to 20 years of the Takeovers Panel

First, in Airline Partners' bid for Qantas in 2007, the bidder declared that its offer price was 'final' as soon as the bid was announced. As matters progressed, it was apparent that the price would not be enough to get the bidder to its targeted 90% ownership threshold, particularly as two institutional shareholders were vocal in saying that they considered the shares were worth more than the bid price.

The bidder then relied on the tactic of saying the bid would close at 7pm on a Friday evening, unless it received acceptances for at least 50% of the shares by then. Unfortunately, due to what may have been a technological hitch, an acceptance for a significant parcel of shares was delayed and did not reach the bidder until several hours after the deadline, leaving the bidder under 50%. The bidder, looking down the barrel of an unsuccessful bid, applied to the Panel for a declaration that closing the bid would be unacceptable. Over the course of the weekend, the Panel and a review Panel decided that there was nothing unacceptable by closing the bid in accordance with the bidder's prior statement. When shares resumed trading on the Monday, the market was fully informed.

It was a great example of how quickly the Panel can act. It upheld the market integrity principle, even where that prevents shareholders from selling their shares into a bid.

Truth in takeovers was also was at stake in Cemex's A$17 billion cash bid for Rinker, one of the largest cash bids ever undertaken in Australia. Rinker had declared its bid price 'best and final' after negotiating with the target directors to secure a recommendation. However, a key shareholder indicated that it would still not accept the bid unless it was sweetened even further. So Cemex agreed with Rinker that Rinker would pay a 25 cents per share fully franked final dividend and Cemex would not exercise rights under the offer documentation to deduct that from the offer price, effectively giving shareholders an additional 25 cents per share.

ASIC brought the matter before the Panel which declared that unacceptable circumstances had been caused by Cemex effectively departing from its 'best and final' statement. However, as over 70% of shares in Rinker had already been accepted into the bid at this stage, the Panel decided that the best outcome was to order compensation to shareholders who had sold their shares on market between the date of the bid being declared final and the date the dividend was announced. This was upheld by a review Panel, by the Federal Court and then by the Full Court of the Federal Court.

The truth in takeovers principle is not found in legislation nor have the courts ever enforced it. The market has the Panel to thank for the rule being followed.

Shareholder intention statements

It has long been common practice for a bidder to sound out shareholders privately about whether they would accept a bid if made at a particular price. In many instances, to give the bid momentum, the arrangement is, with the consent of the shareholder, made public at the time the bid is announced.

Controversy emerges where the percentage of shares involved exceeds 20%. Views have been expressed that, given these statements should be followed consistent with the truth within takeovers principle, the statements were tantamount to giving the bidder a 'relevant interest' and, if the number of shares exceeded 20%, this would breach the takeovers legislation.

To deal with the issue, the Panel issued guidance in 2015 that, provided the shareholder reserves the right to sell into a superior bid and does not accept the bid for 21 days after the offer opens, such statements are acceptable and consistent with the objectives of the legislation.

This guidance has clarified an important part of market practice, showing again that the Panel can play a role as an effective rule-maker.

I have identified just five developments in the last 20 years of the Panel. There are many other examples of the Panel's work which could equally have been mentioned. The Panel has brought about significant and positive change to our market and improved Australia's standing as a destination for capital and investment. Its great success would exceed the hopes of everyone who championed its creation.

Rodd Levy is an M&A Partner of Herbert Smith Freehills and was a member of the Takeovers Panel 2007-2019. He is a member of the Panel's committee reviewing the guidance note on disclosure of equity derivatives.

Tony Damian

Reflections on 20 years: an interview with Allan Bulman

Tony Damian met with Allan Bulman, Director of the Takeovers Panel, to discuss and reflect on the development, progress and success of the Panel over the last 20 years.

Q 20 years on, over 500 applications[1] later – here we are – any high level observations on the Panel's first 20 years?

AB: The Panel has provided bidders, targets, shareholders and other interested parties with the opportunity to be heard in a fair, prompt and cost effective manner. This has had the effect of freeing up considerable court and ASIC resources.

The Panel has considered a number of difficult and high profile applications, including (but not limited to) – Goodman Fielder (2003), Qantas (2007), Rinker (2007), Foster's Group (2011), Billabong (2013), Affinity Education (2015) and Spotless (2017). It has also considered numerous other applications in relation to a wide range of companies. Over a third of applications are now from shareholders and in a number of cases they have been successful in bringing issues to light and ensuring that unacceptable circumstances have been remedied.

I am of course biased but I consider that the Panel has been a resounding Australian regulatory success story, particularly in terms of substantially increasing productivity and reducing the costs associated with takeovers dispute resolution.

Q I think on any fair assessment the Panel has been a remarkable success. What do you think have been the keys to that success?

AB: Ten years ago Professor Ian Ramsay identified 15 reasons for the Panel's success up to that point.[2] While all those reasons still apply today, the reasons which resonate the most with me are:

- The strength and membership of the Panel – we have been fortunate that the government has supported the Panel by appointing outstanding lawyers, investment bankers, company directors and other market participants to the Panel
- The timeliness of the decision-making of the Panel
- Access to the Panel – Professor Ramsay noted that the fee to make a Panel application (currently A$2400) compares favourably to commencing litigation and that the prompt nature of the Panel's decision-making process combined with the Panel's preference for parties to be represented by their commercial solicitors reduces the costs to parties
- The Panel's informal and non-legalistic approach to resolving takeover disputes – including adopting a principles based approach and ensuring where possible that a takeover bid proceeds so that target company shareholders can consider the bid
- The support the Panel has received from the government – in addition to Panel appointments, Professor Ramsay noted that the government responded promptly to amend the Corporations Act when two Court decisions in 2006 and 2007 threatened the efficient operation of the Panel. Professor Ramsay also noted that the Panel had a budget that was sufficient for it to undertake the functions it is given under the legislation (which remains the case)
- The effective leadership of the President of the Panel and the expertise of the Panel executive – in particular we have been fortunate to have been led by outstanding Panel Presidents, Simon McKeon AO (1999 to 2010), Kathleen Farrell (now Justice Farrell, 2010 to 2012), Vickki McFadden (2013 to 2019) and Alex Cartel (2019 to present)

Q On average I think it's around 16 or so days between an application and a decision – how have you managed to hit those sorts of timeframes, especially given that I imagine some time is taken clearing panel members for conflicts in a particular situation?

AB: You have correctly identified the appointment of sitting Panels as one of the main risks to deciding Panel applications promptly. Over my time at the Panel we started recommending to the President that we approach more Panel members and sometimes we approach the entire Panel membership where many Panel members are likely to be conflicted. Also the government has appointed some Panel members who are less likely to be conflicted, which also assists.

The Panel's *raison d'être* as a commercial peer review body provides an impetus to decide applications promptly. Parties usually want applications in relation to bids and rights issues to be decided promptly. Also the effect of the time limits in the legislation means that the Panel usually only has a month from receipt of an application to make a declaration of unacceptable circumstances (without receiving an extension of time from the Court). This can put a lot of pressure on the Panel in relation to complex applications, including in relation to association.

By the way, you may be interested to know that while on an annual basis the average number of calendar days from application to decision varies (mostly because the proportion of matters where the Panel conducts proceedings varies from year to year), the long term average of approximately 16 calendar days has been relatively constant.

1. The exact number as at 24 February 2020 is 568.
2. Ian Ramsay, 'The Takeovers Panel – A Review' in Ian Ramsay (ed), *The Takeovers Panel and Takeover Regulation in Australia*, at pages 13 – 14.

Tony Damian
Reflections on 20 years: an interview with Allan Bulman

Q Back in the early days, we had some sagas in the Panel that seemed to spawn endless proceedings. We had Taipan that got up to 10 applications, Normandy that was 7 – we don't seem to see that as much anymore – why do you think that is?

AB: I have to admit that recently we have had multiple applications in relation to Molopo Energy and Benjamin Hornigold, which may in part be due to the 2019 being the second busiest year on record for the Panel (dealing with 38 applications).

Whether the Panel receives multiple applications in relation to the same entity or transaction is predominately outside the Panel's control. If the Panel declines to conduct in relation to a higher proportion of applications, this may deter multiple applications in relation to the same entity or transaction. From 2000 to 2009, the Panel declined to conduct in approximately 32% of applications. From 2010 to 2019, the Panel declined to conduct in approximately 41% of applications. My reflection on this increase is that the Panel has become more confident in its judgment in considering the merits of an application.

Another possible factor is that shareholder applicants are less likely to make multiple applications. As noted above more than a third of applications in recent years were made by shareholders.

Q When the Panel started people looked at the London model and we all wondered whether the stigma of a declaration of unacceptable circumstances would be enough. In my personal opinion, I think the deterrent has been less of the stigma but more of the consequences given the Panel's broad powers, but how do you see it?

AB: I consider that the effect of the shift in the legislation from 'unacceptable conduct' to 'unacceptable circumstances' was to remove the stigma of a declaration. As mentioned by two members of the High Court in *Alinta*, a declaration is now a statement that 'something needs to be done' in relation to a set of circumstances. This is consistent with the Panel's powers which are remedial in nature. It is also consistent with the statement I made to the media when I was appointed Director in 2008 that it is not the Panel's role to punish market participants but rather to remedy unacceptable circumstances, which is now reflected in Guidance Note 4: Remedies at paragraph 5.

The UK and Hong Kong Panels have a power to make 'cold shoulder orders' in relation to persons who contravene their respective codes. Giving the Panel the power to make 'cold shoulder orders' would arguably be useful in ensuring compliance with the takeovers provisions. However the Panel's operations and processes would need to change substantially to ensure that it could give sufficient procedural fairness in the exercise of such a power.

Q How well and how quickly did the market adapt to the fact that the Panel was different to Court? What do you think has changed in the way parties go about approaching the Panel?

AB: The strong preference of the Panel early on to only allow a party's commercial lawyers to represent them in Panel proceedings in many ways forced market participants to adapt.

Sometimes the relatively informal nature of Panel proceedings can lead parties to make emotive and hyperbolic statements in their submissions. This is a mistake. Panels are more likely to be persuaded by clear and logical submissions rather than submissions based on emotion.

Q You don't have contempt powers – so how do make sure that parties play ball and observe the rules?

AB: Misleading the Panel and contempt of the Panel are both offences (see ss199 and 200 of the ASIC Act) but the Panel cannot off its own bat enforce them. The Panel can make interim and, if it makes a declaration, final and costs orders in relation to a party's conduct in a proceeding (when the Panel has the power to do so). The Panel can also refer matters to ASIC for investigation (including for contraventions of the above sections).

That said, the instances where parties don't play ball and observe the rules in a serious way are at the margins.

Q Early on there was concern about precisely how the relationship between the Courts and Panel would work. What are your thoughts on how that's played out?

AB: I think there has been a growing realisation by the market that the powers of the Courts and the Panel are fundamentally different and therefore there is no inherent conflict between them. As noted by Justice Goldberg in Tower Software Engineering Pty Limited; Pendant Software Pty Limited v Harwood [2006] FCA 717 at [43]-[44]:

- The Federal Court is not seized of the determination of all the issues raised by Mr Hoff before the Panel; it is seized of the issue whether the directors have acted in a way which invokes s 1071F of the Act. Although the Court has to determine whether the directors were, on 11 May 2006 and prior thereto on 4 May 2006, entitled to refuse to agree or consent to the registration of the transfer from Equity Partners, the Court is not set at large upon the sea of the takeover offer, although it can determine whether the directors had just cause to refuse to agree or consent to the registration of the transfer. If there be any unacceptable circumstances found in the lead up to an implementation of Pendant Software's takeover offer then it is for the Panel to tease those out and make declarations in relation to them. That is not a task committed to the Federal Court under the Act

- If there be such unacceptable circumstances found which the Panel determines have an effect or consequence upon the transfer from Equity Partners to Pendant Software then that decision or declaration is not impinging upon the jurisdictional turf of the Federal Court. It is a consequence of the Panel undertaking the task identified by Emmett J in par [56] of his judgment in Glencore (supra). It is not the Panel making a decision on, or a declaration in relation to, the issue of the obligation of the directors on 4 or 11 May 2006. The consequence of the Panel's determination may be to remove the substratum of the basis for the registration of the transfer sought by Pendant Software, but that is not because of the Panel assuming the task of the Court or destroying the substratum of the matter before the Court. It is because there is a separate and independent basis for a challenge to the consequences of the carrying out and implementation of Pendant Software's takeover offer

Q Any thoughts on the Panel's role in developing policy through its guidance notes? I remember the anticipation around the 2001 lock up devices guidance note. The insider participation note of 2007 was probably another big one.

AB: Our 18 guidance notes, including the ones you have mentioned, have provided market participants with useful guidance about their obligations and improved compliance.

On a number of occasions, the release of a guidance note by the Panel has led to a reduction in applications in relation to the subject of the guidance note. This is particularly pronounced in relation to the Panel's guidance on disclosure (see in particular Guidance Note 14 – Funding Arrangements, Guidance Note 18 – Takeover Documents and Guidance Note 22 – Recommendations and Undervalue Statements). It can also be seen (after a number of attempts) in relation to the Panel's recent rewrite of Guidance Note 17 – Rights Issues.

The Panel is constantly reviewing its guidance notes. It is close to finalising a rewrite of Guidance Note 20 – Equity Derivatives and will shortly commence a review of Guidance Note 19 – Insider Participation in Control Transactions (which has been considered in a number of recent Panel decisions).

Tony Damian
Reflections on 20 years: an interview with Allan Bulman

Q Has the Panel had many conferences, and is that something you think will ever become more common?

AB: The Panel has conducted 12 conferences in its history (5 in the last 10 years). From my experience as a participant (on behalf of ASIC) and later a member of the executive, conferences particularly have a place where parties desire a quick outcome and are willing to participate in the conference process.

While obviously infrequent, I think that the Panel will continue to conduct conferences from time to time.

Q Are there any standout moments in your 12 years as Director you can share?

AB: I feel a little bound to confidentiality in relation to some matters – 'what is said at the Panel stays with the Panel'. Certainly working on complex and interesting matters such as Billabong, Ross Human Directions, Yancoal and recently ERA has been very rewarding for me professionally. Many of our matters also have had some interesting (and dare I say entertaining) revelations and 'twists and turns'.

I would like to add that working with a selection of the best practitioners in the field is a constant pleasure. This includes the Panel members, executive and experienced practitioners such as yourself.

Q Any bold predictions about what the 40th anniversary of the Panel might look like?

AB: I have recently been reflecting on a Harvard Business Review article that studied organisations (including the New Zealand All Blacks[3]) that have stood the test of time.[4] Factors that the authors consider are important include having a stable purpose and stewardship, being open and transparent and having a 'disruptive edge' (being an ability to hold to traditions while at the same time striving for innovation).

While we are small the Panel's culture shares some similarities with these impressive organisations. Will the Panel be around to celebrate its 40th anniversary? That is a decision for government and is ultimately out of our control. But the Panel membership and executive can develop our capabilities to continue to be relevant as a peer review body for takeovers assuming that this role continues to be required.

Many practitioners, including Rodd Levy, have suggested an expanded role for the Panel. Again, those decisions are matters for the government and will depend on market and political trends which I cannot predict. However if I were to guess we are likely to be celebrating our 40th anniversary as a continued success.[5] We have recently started using data rooms for the receipt of material for matters. I am pretty confident that this trend will continue and that IT solutions (including artificial intelligence) will be a crucial part of the Panel's work in 2040.

The views expressed in this interview are the personal views of Allan Bulman.

Tony Damian is an M&A Partner of Herbert Smith Freehills. He is a co-author of Schemes, Takeover and Himalayan Peaks, a leading book on public company mergers.

3. Noting my wife is a Kiwi!
4. Alex Hill, Liz Mellon and Jules Goddard, 'How Winning Organisations Last 100 Years', *Harvard Business Review*, 27 September 2017.
5. I mean 'we' to be the Panel as an organisation. I can boldly predict that I will not be working at the Panel in 2040.

Rebecca Maslen-Stannage

Litigation unplugged, takeover disputes reimagined and the rise of 'the vibe'

Twenty years ago, I did the unthinkable as a Herbert Smith Freehills Litigation partner. Over lunch one day chatting to a Herbert Smith Freehills takeovers great, I defected to the Herbert Smith Freehills M&A practice group. I have been a M&A partner with the firm ever since.

In the lead-up to my defection, I had been involved in numerous takeover disputes – that was what a corporate litigator did at the time. I thoroughly enjoyed the sport of injuncting the despatch of 'Part A' or 'bidder's' statements. It was a matter of pride to see how long we could delay that despatch. This was not just a sport. A target company suddenly faced with a hostile bid – a relatively common occurrence at the time – tactically needed to buy time to get onto the front foot. Delivering only the occasional rebuke about 'tactical' litigation, generally judges seemed to enjoy these cases, so they could often be brought within a tight time frame. However, there was still ample opportunity to cause delay and embarrassment to the bidder in an early strike back for the target.

I was disappointed that the change in law benched the courts in takeovers before I had a chance to achieve the holy grail of causing a printed bidder's statement to be pulped. However, I had played my part in making bidders delay their despatch and making some pretty ugly disclosure.

Litigation unplugged

My move from litigation to M&A was not driven by the establishment of the Panel as we now know it or the consequential benching of the courts on takeover disputes. But that proved to be a happy coincidence.

I had become frustrated with the artificial strictures of the rules of evidence and procedure. I had a philosophical objection to the rule against hearsay.

So how happy was I to discover the new Panel world where the rules of evidence did not apply? The idea was originally that investment bankers, rather than lawyers, would be the voice of the parties before the Panel, inspired by the London experience. I'm not sure anyone had consulted the Australian bankers. It turned out that the investment bankers were not keen to be the submission-makers before the Panel. M&A lawyers tend to have strong views and the wish to express them vocally, so we happily stepped into that void.

> The idea was originally that investment bankers, rather than lawyers, would be the voice of the parties before the Panel, inspired by the London experience. I'm not sure anyone had consulted the Australian bankers.

Most M&A lawyers don't know the rules of procedure or evidence. I enthusiastically disavowed my legacy knowledge in my new role as gamekeeper turned poacher – and embraced the new takeovers world order – which turned out to be 'litigation unplugged'.

Some lawyers clung for a while to litigation concepts in submissions. But not us. There was no creative argument we could come up with which we couldn't find some form of hearsay evidence to support – always within the bounds of professional responsibility of course! Affidavits and formal evidence became superfluous, giving us licence to illustrate our points with appropriate colour and flair.

We were all feeling our way in the early days of the Panel. We had our wings clipped on occasion in the early post-matter reviews, with suggestions that more temperate language and less hyperbole would be received favourably by the Panel. It was hard to separate what had 'got us a win' from our expression. We didn't want to move to express ourselves like litigators, but we resolved to be more 'statesmanlike' in our future tone.

The rise of 'the vibe'

While the method was more fun in the world of litigation unplugged, some of the victories became less satisfying. While the courts had been strong on principle with plenty of scope for technical arguments, the Panel proved to be more about substance than form or detail. There were early pyrrhic victories where the Panel accepted that bidder disclosure was misleading and required corrective disclosure – only to have the bidder use the corrective disclosure for its own propaganda purposes. Then there was the dreaded 'self-help' response: 'A problem with bidder disclosure – why can't you fix it yourself by what you say in your target statement?'

It is fair to say that the Panel reimagined takeovers disputes. The courts focus primarily on rules – albeit having regard to the Eggleston Principles (equal treatment, information, to name a couple). However, in the Panel 'the vibe' of the Eggleston Principles trumps technical legal rules.

Rebecca Maslen-Stannage

Litigation unplugged, takeover disputes reimagined and the rise of 'the vibe'

The new Panel certainly did not perceive itself as a quasi-court – as the Review Panel in Pinnacle 08 signalled loud and clear:

> **The commercial community is seeking in the Panel, not for a second-rate court, but for a first-rate commercial Panel. It should not therefore ... attempt to replicate court processes, thereby unduly delaying fast-moving transactions and the bid itself.**

Instead of a win/lose scenario, the Panel quickly became known for 'something for everyone' outcomes – with target shareholders typically emerging as winners. It is often said that the Panel favours getting bids and information before shareholders so that they can decide.

The cases where it became most stark that takeover disputes under the Panel regime had been unplugged from the past, or reimagined, were those which no court would even have had the power to make decisions which were inconsistent with legal rights but consistent with 'the vibe' of the Eggleston Principles. Pinnacle 08 woke the market up to what had actually been created in the Panel. The Panel could, and did, create new rights to further the Eggleston 'vibe' – in that case by constraining frustrating action without even having to decide the classic court question whether directors had breached their duties. Another high water mark was the Centro v AMP Shopping Centre Trust case – where the Panel was prepared to order a party to a contract not to exercise its contractual pre-emptive rights because the target had not disclosed those rights to the market.

20 years of the Panel

The takeovers world has generally become more benign over the past 20 years, with less hostile bids and indeed less major takeover bids. Major takeovers tend to be implemented with the scheme of arrangement structure which, while it can be preceded by a 'bear hug', is ultimately target-driven. It is hard to separate cause from effect in terms of the Panel's role in this. At a minimum, parties are more willing to compromise because they perceive that a middle ground is the likely outcome of Panel proceedings and that technical arguments will not lead very far. Actions by shareholders and other 'fringe players' may lead to future growth in Panel activity – always if they can be put consistent with 'the vibe' of the Eggleston Principles.

The Panel has also established a rhythm in terms of managing evidentiary issues. The Panel remains appealingly process-light, but we wouldn't expect great sympathy from the Panel in an association case without evidence of a better quality than hearsay.

So twenty years on, it's 'the vibe'. It's about sensible and timely decision-making, not stymied by technical and procedural requirements. It is still fun – albeit with less sport involved than in the old days. And there's no doubt that target shareholders have benefited from the Panel's progress, over 20 years now, in reimagining takeover disputes to further an efficient market where offers reach shareholders and ultimately shareholders get to decide.

Rebecca Maslen-Stannage is an M&A Partner of Herbert Smith Freehills and has been a member of the Takeovers Panel since 2017.

George Durbridge

Can I see the Panel? Reflections on Panel practice and procedure

We hear that in London, when the London Panel on Takeovers and Mergers has to sit, the members proceed to the Panel offices at the end of the day, and together hear oral submissions. The procedure is civilised, personal, quick and efficient. Why, then, do proceedings in our Panel generally proceed by emails and attachments, with the parties never fronting the Panel, although the Panel has power to hold a conference?

Time and space

All of the Panel members, and all of the bankers and lawyers who might be required at a sitting of the London Panel will work within the notional Square Mile of London. By contrast, participants in Takeovers Panel proceedings in Australia may be scattered over 3 million square miles.

A sitting Panel comprises three members. The three Panel members sitting on a matter are almost always based in different cities. In the five years I served as counsel to the Panel, we had one Panel whose members were all based in one city.[1] The reasons for this are pretty basic. The Commonwealth Government appoints members to the Panel on the basis that each possesses relevant experience or expertise, and that between them they represent all of the major commercial centres in Australia. The substantive President appoints members to sit on a particular Panel on the basis of a spread of expertise (for instance, one lawyer, one banker, and someone who understands accounts), absence of conflicts, availability and sharing the workload between members. That leaves virtually no scope to appoint three members from the same city.

Although two of those members constitute a quorum, Panels generally prefer all three members to be present for any substantive proceedings. For one member to be absent detracts from the combination of skills and experience which the President attempted to achieve in appointing a particular sitting Panel. If one member must be absent for part of a matter, the other two members may continue the proceedings. However, it is much fairer to the parties for only two Panel members to continue the matter if both of them have been present for all previous stages.[2] The cost of that is, however, that Panel proceedings can only be carried forward when matching gaps can be found, or more often made, in each member's schedule.

For a one-hour discussion by telephone, that involves each member giving up an hour (plus reading time). For a one-hour face-to-face hearing, it means one or two members taking the time for a taxi, a flight, and another taxi (and perhaps finding time to read the relevant papers on the plane). Basically, a day away from the office. The extravagance of a full day's sitting can sometimes be justified if, for instance, a matter which might otherwise run on for several days can be dealt with in one day, or if it seems advisable to take the *viva voce* evidence of a critical witness. But it usually cannot be justified, and when it can, it often takes so long to free up matching days that it actually delays the resolution of the matter.

That extravagance is mainly incurred by the member, not the taxpayer, as the amount the Panel pays for their time is a fraction of the amount they might have billed for it in the ordinary course.

Substance

In general, a Panel matter doesn't raise the sort of issues for which an oral hearing is needed. It rarely involves disputed law, or even contested evidence. The applicable law is fairly familiar (even if it is not entirely clear around the margins) and its policy is usually well understood. The Panel has only once referred an issue of law to court, and that issue did not concern takeovers or administrative law, but the construction of a trust deed. Very often, all of the relevant evidence is derived without objection from annual reports, substantial holder notices and other company documents or lodgements with the ASX.

1. Even then, the parties were in another city. Personal recollections relate to George Durbridge's experience as a member of the Panel Executive from 2000 to 2005.
2. There are limits on how far a member can be brought up to date on proceedings in their absence: *Jeffs v New Zealand Dairy Production and Marketing Board* [1967] 1 AC 551, [1966] NZPC 1.

Provided evidence of that kind isn't taken out of context, it can be provided as well by cutting and pasting as in any other way.

Of course, the Panel doesn't always have the evidence it needs, but the missing evidence is usually hiding behind obfuscation concerning relevant interests, associations and the like. For instance, in Brockman Resources Ltd, a serious effort by private detectives unearthed a lot of circumstantial evidence which pointed strongly to a concert, though not strongly enough to satisfy the sitting Panel. If there is evidence fit to put to a witness in cross-examination, the evidence is fit to put to the Panel to raise a doubt over that person's narrative.[3]

Process

Panel proceedings are not a suitable venue for indulging your Perry Mason aspirations. The Panel's procedures are more inquisitorial than adjudicative. That is, parties do not run their own cases by first lodging pleadings and then developing their cases in accordance with those pleadings, but otherwise as they see fit. Instead, the ASIC regulations require the Panel to take control of the proceedings, by issuing a brief and requiring each party to lodge a submission which addresses questions posed by the brief. Parties may then make a second round of submissions in rebuttal. This process may be repeated as necessary: in particular the Panel commonly issues a supplementary brief on orders.

That isn't the whole story. A party may provide the Panel with submissions which it has not invited or add to a submission a discussion of issues which, in its view, the brief overlooks. On a number of occasions ASIC has volunteered information which it has acquired under notice.

This procedure has a number of advantages. It ensures that submissions arrive in a form which is congenial to Panel members, most of whom are unaccustomed to litigation. It informs the parties as to the issues which the Panel thinks are raised by the application, with some opportunity to ask it to change its focus. It allows each party to spend a couple of days researching and setting out its response to the issues as formulated by the Panel. It allows them another day to respond to how the other party or parties have addressed the same issues.

It also draws on the particular strengths of solicitors. It requires preparation and writing skills, rather than readiness on your feet, which is a particular requirement of barristers. By using its power to consent to legal representation, the Panel is able to ensure that submissions are usually prepared by the solicitors who are acting in the relevant matter, and who have prepared the documents and already thought about the issues.

The Panel's power to hold a conference is supplementary to its obligation to seek and consider written submissions, however, because the functions of a conference are to clarify matters already before the Panel, and resolve inconsistencies between them. A conference is not an opportunity for a party to take control over the direction of the proceedings. The Panel must provide to each person who may attend the conference a statement of the matters which the Panel proposes to raise at it, and may disregard other matters.

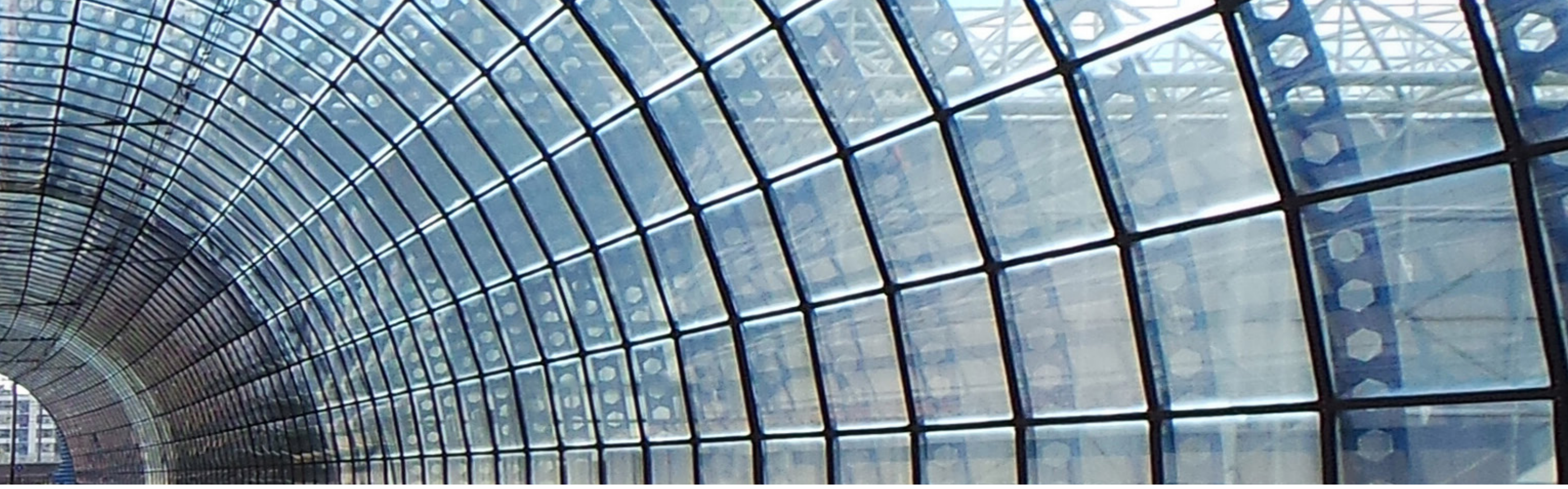
Telephones

In addition to the sitting members and the solicitors acting for the parties usually being based in different cities, they invariably have crowded appointment books.[4] It is always difficult to find matching gaps in Panel members' schedules for telephone conferences, but when you add the travel time for a face-to-face meeting, it often becomes impossible, without postponing a decision unacceptably. A face-to-face meeting with even one party is even harder to arrange, but of course you don't want just one party: you want them all, so that each can hear what the others say.

As a result, most Panel meetings were held by telephone conference. The Panel's equipment is high quality, as these things go, but a teleconference just isn't as effective as a face-to-face discussion. It was generally impossible to marshal three members for a teleconference in

3. In another matter, however, polite but persistent questioning by the Panel reduced the former company secretary of the target to tears. Nobody wants to see that again.

4. One (stalwart) Panel member was sometimes known as 'Adelaide', but he was based in Sydney, and confessed to having received the nickname from being perennially half an hour late.



business hours. Most telephone conferences were after hours, though some were at lunchtime or early in the morning. Members really put themselves out to ensure they are available. Teleconferences proceed best with a written agenda or statement of issues, but the more urgent the meeting, the less time there was to write or read a paper. Occasionally a member who was in Melbourne would attend a conference call from the Panel's office, or two would get together in Brisbane or Adelaide: that always made the conference noticeably easier to follow for all concerned.

Skillset

Some conferences work, and others don't. The sitting President, who must run the conference, really needs to be accustomed to preside. For example, one conference presided over by a commercial silk was a model of polite but ruthless efficiency, structured and timetabled to the nearest minute. Very polite, very firm, and quite fair. The late Kim Santow (then a judge of the Supreme Court of New South Wales) ran a short telephone conference, having confined the issues on which parties might speak and limited their time, and sorted out those issues in just over an hour. By contrast, another conference run by a competent commercial solicitor with two other very capable members and (I think) no litigation experience between them wandered on into the night with no end in sight, until a chance remark enabled a couple of us to call for a short break.

Assessment

In Pinnacle 08, the sitting Panel observed that the Panel's powers and procedures enabled it to decide confidently, and in time to be of value to shareholders, that unacceptable circumstances had occurred, and had been remedied. That was one of the reasons why they declined the parties' invitation to consider whether those events had also involved a breach of directors' duties, that being something which would require the time and powers available to a court.

In that context, they pointed out that:

- 'The commercial community is seeking in the Panel, not for a second-rate court, but for a first-rate commercial Panel. It should not therefore fall between two stools and attempt to replicate court processes, thereby unduly delaying fast-moving transactions and the bid itself.'

The limitations on Panel procedures are concomitants of the attributes which make it focussed and effective. That should be borne in mind in any evaluation of the Panel or in consideration of changes in the Panel's composition or functions.

George Durbridge is a Special Advisor at Herbert Smith Freehills and was lawyer with the National Companies and Securities Commission from 1986 until 1990, and General Counsel of the Australian Securities Commission from 1991 until 2000, mostly working in takeovers. Between 2001 until 2005 George was Counsel of the Takeovers Panel.

Philippa Stone

Back to the Future – developments in the Panel's approach to rights issues

It is interesting to reflect on how the Panel's approach to rights issues has changed over its 20 year life in its current form. Initial Panel guidance adopted a presumption of acceptability, but over time the Panel became more interventionist in practice, finding unacceptable circumstances in a large number of rights issues.

More recently, and in particular since the 2018 revisions to Guidance Note 17 (and the consultation leading up to that Guidance Note), the Panel has reverted to a less activist approach, particularly where a clear need for funds can be shown. However, recent decisions like those in relation to Energy Resources of Australia Limited (ERA) show that the Panel will still intervene where it has concerns with the rights issue process, particularly where the Panel believes there may be a control purpose.

Initial Panel guidance – a presumption of acceptability

Numerous decisions of the Panel since its inception have tested and shaped the Panel's approach to rights issues (and the related exceptions from the takeovers provisions in items 10 and 10A[1] of section 611 of the *Corporations Act 2001* (Cth) (Corporations Act) and the potential for unacceptable circumstances to exist as a result of them.

By the time the Panel came to consider issuing its first standalone Guidance Note on rights issues in 2004, more than 10 matters had come before it challenging rights issues on the basis that they gave rise to unacceptable circumstances. Since that time, the Panel's guidance on rights issues has been through a number of revisions, including a complete re-write in 2010 (along with other Panel guidance) and more recently in 2018.

In its first rights issue Guidance Note, the Panel expressed the view that where a rights issue was structured to fall within the relevant exemptions in section 611 of the Corporations Act, there was a 'rebuttable presumption that it was not unacceptable'.

The Panel commented that companies are entitled to manage capital in a number of ways, that informed and rational shareholders who have the opportunity to participate in a rights issue may choose not to participate (with the natural control consequences that flow from that), and that dilution following a choice not to participate in a rights issue was an inherent risk of investment in a listed company. These were sensible observations.

However, the Panel acknowledged that where there was a potential control impact, there was an 'onus' on the board to take steps to minimise that potential impact, and nominated a range of factors as relevant to its assessment of unacceptability including:

- need for funding, with the onus on the complainant to demonstrate there was 'no need for funds or that a rights issue was not the appropriate mechanism'
- structure, pricing, renounceability and shortfall dispersion facilities

Moving away from the presumption of acceptability – the balancing act

When the Panel's rights issues Guidance Note was re-written in 2010, the Panel's published guidance moved away from the concept of a 'presumption of acceptability' in the published guidance and instead presented a range of 'factors' which would be taken into account in considering whether, as a whole, unacceptable circumstances arose in connection with a rights issue. The Guidance Note also included some commentary on safeguards to mitigate control effects. While the onus clearly still rested with applicants to demonstrate a basis for intervention by the Panel, the revised guidance appeared to represent a shift from effectively providing issuer boards with the 'benefit of the doubt' – reflected in the 'acceptability presumption' in the original guidance – to a broader balancing act where a range of competing control factors would be taken into consideration.

A major focus for the Panel in its decisions in this space has been balancing the pressing and genuine commercial imperatives facing listed companies needing to raise funds (often in difficult circumstances), the control effect of the rights issue, and the extent to which adequate measures have been employed by the issuer to mitigate any such control effects.

1. Inserted by ASIC Corporations (Takeovers – Accelerated Rights Issues) Instrument 2015/1069.

> Recent decisions show that the Panel will still intervene where it has concerns with the rights issue process, particularly where the Panel believes there may be a control purpose.

The Panel's deliberations over Yancoal's two separate rights issues in 2014 and 2017 provide a useful illustration of its approach to this balancing act, particularly in the context of 'heavy' rights issues, and appear (among other decisions around that time) to have informed the recent changes to guidance on rights issues.

Yancoal 1.0 (2014)

Yancoal's first Panel encounter occurred in connection with its 2014 proposed rights issue of US$2.3 billion of subordinated convertible notes (SCNs).

At the time, Yancoal was heavily geared, with around US$2.6 billion owed to Bank of China through secured facilities and nearly US$2 billion owed to Yanzhou (a 78% shareholder in Yancoal at the time) through shareholder loans which ranked equally with the Bank of China facilities. Coal prices were falling and during the course of 2014, Yancoal's own projections of its cash flow shortfall between 2014 – 2018 grew from A$600 million to A$1.8 billion. In October 2014 it was forced to seek waivers from Bank of China from compliance with its gearing ratio and net worth covenants, and it was expecting to fail to satisfy these covenants again when they were next due to be tested on 31 December 2014.

It was against this backdrop that Yancoal in November 2014 announced a pro-rata, renounceable rights offer of 2.32112 SCNs for every 100 Yancoal shares, to raise up to approximately US$2.3 billion. Yancoal was proposing to use US$1.8 billion of the proceeds to repay the senior debt owing to Yanzhou and use any remaining proceeds for its existing operations. The rights offer was not underwritten. The SCNs were:

- issued at US$100 per note
- convertible into Yancoal shares at a conversion price of US$0.10 per share
- perpetual (in that they did not have a fixed maturity date and did not have to be redeemed except on a winding up of Yancoal or the issuer, which was a Yancoal subsidiary)
- to receive distributions (initially at 7% per annum) which were perpetually deferrable, non-compounding and within the Yancoal board's control
- subordinated to Yancoal's other debt, but had priority over Yancoal's ordinary shares and a new US$807 million loan that Yanzhou had committed to provide

As part of the package, Bank of China agreed to extend its US$2.6 billion facility, extend the first covenant test date and treat the SCNs as equity for the purposes of the financial covenants under its facility. Yanzhou had committed to take up its entitlement of SCNs in full, and it was noted in the proceedings that if no other shareholders took up their rights, Yanzhou had the potential to acquire up to 98.8% of the shares in Yancoal by converting its SCNs

Philippa Stone

Back to the Future – developments in the Panel's approach to rights issues

over time, relying on the creep rule in item 9 of section 611 of the Corporations Act.

A number of shareholders (including Noble Group) complained to the Panel that (among other things) the rights issue was a 'control play' designed to avoid shareholder approval and provide a mechanism for Yanzhou to compulsorily acquire Yancoal's minority shareholders' shares. It was also contended that the structure of the rights issue did not adequately mitigate the control effects, and that Yancoal's need for funds did not justify the rights issue in the form announced.

The Panel ultimately made a declaration of unacceptable circumstances, although allowing the rights issue to proceed on certain conditions. The key findings which led the Panel to that decision were that:

- the SCNs would have a control effect with respect to Yancoal, and that the fact that they would only have such an effect if Yancoal chose to convert them did not affect that analysis
- Yancoal clearly had a need for funds, but the need for funds is not a complete safe harbour from the consequences of other unacceptable control effects. The Panel suggested that the need for funds was 'less clear than in other rights issues when the Panel has allowed a highly dilutive rights issue with a control effect to proceed' (this seemed slightly difficult to understand, given Yancoal's demonstrably difficult financial circumstances, although the Panel referred to the Multiplex rights issue in 2009, where lenders had more explicitly threatened to call their loan funding)
- Yancoal had not given sufficient consideration to alternative financing structures (or at least was limited in the alternative options it could pursue because Yanzhou would not support alternatives other than the issue of SCNs)
- the rights issue (at an effective ratio of 23:1) was more dilutive than many other rights issues the Panel had previously declared unacceptable, and SCNs were unlikely to be taken up by other minority investors
- Yanzhou was receiving a benefit not available to other Yancoal shareholders, because of its ability to effectively set off its loan amounts against the subscription price for the SCNs (although this was also an interesting point given the loan was a callable debt owing to Yanzhou and ranking equally with the bank debt, in a balance sheet which was clearly over-geared)

The Panel ultimately permitted the rights issue to proceed, but on the basis of an undertaking that Yanzhou could not convert its SCNs so as to exceed its existing 78% interest without first obtaining Yancoal shareholder approval.

Yancoal 2.0 (2017)

In 2017, Yancoal needed funds again, to fund its acquisition of Coal & Allied from Rio Tinto, in a transaction which it expected to materially improve its cash flows and overall financial position. This capital raising had a number of features similar to the earlier 2014 issue of SCNs. US$2.35 billion was to be raised through a 23.6:1 renounceable, pro-rata entitlement offer of new ordinary shares – the same quantum of capital and roughly the same dilution ratio as the 2014 SCNs issue.

However, some key differences between the 2017 rights issue and the 2014 rights issue included:

- the securities offered were ordinary shares, eliminating debate as to whether complexities inherent in the SCN structure were adverse to investors
- Yanzhou had committed to only take up US$1 billion of its US$1.83 billion in entitlements. The balance of the offer was underwritten (albeit by persons who included Chinese SOEs which objectors alleged were Yanzhou associates)
- entitlements could be traded on ASX or sold privately
- entitlements not taken up or sold would be offered for sale through a bookbuild process, with any proceeds above the offer price remitted to the renouncing shareholders
- shareholders taking up their entitlement in full could also apply for additional shares at the offer price, and were guaranteed to receive the number of new shares required to maintain their existing proportionate shareholding (and were also likely to receive any additional shares applied for above that level, subject to availability and unless the bookbuild cleared above the offer price)

Yanzhou had also committed to convert as many SCNs as it was able to, and the combined effect of Yanzhou not taking up its entitlements in full and converting its SCNs would be to leave it with an interest in Yancoal of approximately 65%.

Shareholders (again including Noble Group) again complained to the Panel, on a number of grounds including that the entitlement offer was unacceptably dilutive, did not allow minority shareholders a reasonable and equal opportunity to participate, and was prejudicial to the interests of minority shareholders.

On this occasion, the initial Panel declined to conduct proceedings (let alone make the declaration of unacceptable circumstances sought by the agitant shareholders). The Panel found that:

- the control effect was minimal, since Yancoal was a majority shareholder before the raising and would continue to be a majority shareholder afterwards. The Panel found that the objecting shareholders had not, as a matter of fact, made good their allegations of associations with various underwriters
- the dispersion strategies were adequate – the offer was renounceable and included a bookbuild and shortfall facility which gave other shareholders preferential access
- the directors' decision to fund the Coal & Allied acquisition was governed by their directors' duties and applicable ASX Listing Rules (and, to the extent a shareholder considered these had not been complied with, this should be raised with ASX, ASIC or the courts)

The Review Panel, which supported the initial Panel's decision, went further in dismissing the argument from shareholders that the dilutive effect of the entitlement offer was unacceptable. The Review Panel stated that the dilution to shareholders was an 'inevitable consequence' of Yancoal's decision to fund the acquisition of Coal & Allied through an equity raising (and effectively an inherent risk to shareholders who invest in a listed company), that the shareholders' grievances related more to those decisions than to the structure of the capital raising, and that the agitant shareholders had not raised 'any serious objection' to the merits of the Coal & Allied acquisition.

Back to the future – a return to the presumption of acceptability

In early 2018, the Panel consulted on changes to the then current version of Guidance Note 17 on Rights Issues (published in February 2010). One of the principal reasons for updating this Guidance Note was to provide clearer and more definitive guidance on the features the Panel considers would mitigate the potential control effects of a rights issue.

These updates included more detailed guidance on a number of features which had been important in the 2017 Yancoal capital raising, including renounceability and robust shortfall dispersion strategies. Moreover, a key change was the effective re-introduction of the 'presumption of acceptability' in the form of new wording that 'where there is a clear need for funds, a rights issue will generally not be unacceptable provided an appropriate dispersion strategy has been put in place'. In its submissions, ASIC was concerned that the provision of such a detailed list in the Panel guidance, together with the above observation, may be treated by issuers as a safe harbour – effectively a 'shopping list' of features which, if included, provide a path through any challenge on the basis of other unacceptable control impacts.

While acknowledging this concern, the Panel also commented that many of the rights issues which had previously been the subject of declarations of unacceptable circumstances by the Panel would not have found themselves in that position if they had included these features.

The final wording was amended to go part way to address ASIC's concern, and reads:

> **where there is a clear need for funds that has not been contrived, a rights issue resulting in a control effect will generally not be unacceptable (in the absence of other issues) provided the rights issue is structured appropriately and an appropriate dispersion strategy has been put in place.**

This is a good place for the Panel to have landed, and appropriately acknowledges that companies which are in immediate and pressing need of funds (whether because of banking covenant pressures or because of a need to fund a financially transformative acquisition) may have no ability to raise them except through a rights issue, with the associated inevitable risk of control effects. Provided the need for funds is real, and the offer structure including dispersion strategies are reasonable, it is sensible that the Panel should generally stand back and not seek to restructure the parties' transactions unless there are other significant issues in play.

Looking ahead

The coming years will inevitably bring more 'heavy' rights issues, where companies need to raise funds to refinance debt or continue to invest in their operations and future growth. It is obviously important in this context to strike the right balance between intervening to prevent unacceptable circumstances while not interfering unduly with genuine commercial transactions with a proper funding purpose.

The current Panel guidance, the outcome in the 2017 Yancoal applications, and the recent tendency of the Panel to be much more robust in determining not to conduct proceedings unless there is a real prospect of unacceptable circumstances at play (noting that the delay inherent in full Panel proceedings could of itself seriously threaten the viability of many rights issues), all suggest this balance is now being struck in a pragmatic and predictable way. This approach gives appropriate weight to the real commercial funding imperatives and discourages 'gaming'.

However, the recent finding by the Panel of unacceptable circumstances in ERA shows that the Panel will still intervene where it has concerns there may be a control purpose and it is not satisfied with the issuing company's decision making process. That case involved a pro-rata renounceable 6.13 for 1 entitlement offer by ERA to fund rehabilitation obligations.

ERA's 68% shareholder, Rio Tinto, underwrote the offer (and this could, if other shareholders failed to take up their rights, have led to Rio Tinto's holding increasing to 95.6%, and Rio Tinto becoming entitled to compulsorily acquire outstanding shares). The largest of the minority shareholders objected, and the Panel found unacceptable circumstances in relation to a number of matters including ERA's decision making process (essentially, whether an independent board committee established to address related party issues had acted with sufficient rigour). A Review Panel affirmed the initial Panel's declaration of unacceptable circumstances, although reducing the scope of remedial orders.

The ERA decisions show (again) that a real need for funds plus dispersion strategies will not always be enough. A practical lesson that advisers can take away from the decisions is the potential benefit of appointing independent financial advisers to act for an independent board committee (IBC), if the IBC is tasked with making decisions in relation to a rights offer to mitigate potential or actual conflicts.

Philippa Stone is an M&A Partner of Herbert Smith Freehills and has been a member of the Takeovers Panel since 2019.

Clayton James

The Panel, private equity and insider participation

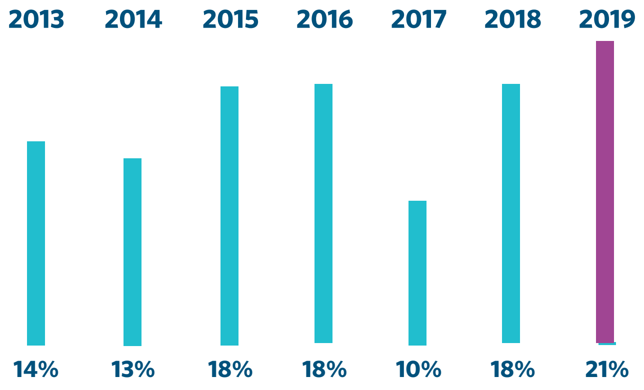
At a time where there is a significant uptick in the number of public to private transactions in the Australian marketplace, it is informative to revisit the Panel's 2007 issues paper and draft guidance note on insider participation in control transactions – and private equity bids more broadly.

The publications were issued by the Panel at a time where there was also a significant number of public to private bids and substantial media, political and academic consideration of private equity and the involvement of management and directors in private equity bids.

Framing the conversation: private equity bids in Australian public M&A

Before considering the Panel's issues paper and response in detail, it is important to recognise the significance of private equity as a contributor to public M&A deal activity. In FY19, 21% of public M&A transactions involved a private equity bidder, compared to 18% in FY18 and 10% in FY17. In FY19, private equity was active across a broad suite of sectors (including healthcare, education, IT/Telecommunications and consumer goods) and also across asset values – from the smaller end of the market through to multi-billion dollar transactions. Importantly, this increasing level of activity is anticipated to be a continuing theme in the Australian market. The robust conditions for public to private bids are driven by record levels of 'dry powder' (undrawn capital commitments from limited partners), strong M&A competition for private assets (manifesting in contested auction processes), low interest rates and the relative political stability of Australia.

The chart below indicates the proportion of M&A deals which involved private equity over the last seven years and shows the surge of private equity activity in FY18 and FY19.



The Takeovers Panel focus on private equity

In 2007, the Panel published an issues paper and draft guidance note (primarily) focused on executive and director participation in control transactions. The issues paper acknowledged that the publication of the draft guidance note was motivated by a series of high profile private equity bids both domestically and overseas during 2006 and 2007. A feature of some private equity bids during this time was the involvement of target executives and board members as part of the private equity bidding entity.

While the focus of the issues paper and the guidance note was insider participation in bids, the scope of the issues paper was broader and considered issues in relation to private equity bids more generally, with these issues reflecting, in part, media reporting of private equity bids at the time.

Against the backdrop, we consider below the various issues identified in the Panel paper, feedback received, and policy position ultimately adopted by the Panel. In framing the issues, the Panel makes abundantly clear in the introduction to Guidance Note 19 (GN 19), that the issues considered are relevant to all bids, and are focused on the circumstances of the bid, rather than the identity of the bidder. Aided by feedback received during consultation, the Panel makes clear in GN19 that private equity bidders should not be discriminated against when applying the Eggleston Principles as against other market participants.

Participating insiders

The crux of the issue for the Panel is the concern that insiders (with the term including officers or advisors able to influence the target's consideration of the bid or who held significant non-public information) who participate in a bid (or a proposed bid) by having arrangements with the bidder, may have a financial incentive to ensure that the bid is successful. The participation by insiders was also linked to a concern that participating insiders may also have an interest in stymying rival bidders, including by curtailing the amount of information provided to rival bidders.

For the purposes of GN19, a 'participating insider' is an insider who has entered into an agreement with, or been given an understanding by, a potential bidder that they will gain a benefit from the bidder making a successful bid. Examples of the forms of arrangements concerning the Panel included equity participation in the bid vehicle and arrangements that will apply if the bid becomes successful, for example cash or fees linked to the performance of the target. Exceptions to the arrangements that may otherwise be caught by the Panel's policy include existing incentive arrangements or new arrangements on similar terms.

Clayton James
The Panel, private equity and insider participation

Addressing conflicts of interest

The issues paper and draft guidance note identified, from the Panel's perspective, a need for processes which ensured that the consideration of the relevant bid and potential rival bids were not materially inhibited by the involvement of insiders. Such processes are to include:

- an obligation on insiders to notify the board of potential change of control transactions
- as soon as the board becomes aware of a potential bid for the company where there is, or is likely to be, participation by insiders, establishing appropriate protocols

Such protocols include the appointment of an independent board committee (IBC) (comprised of non-participating insiders), control over the disclosure of information, taking steps to preclude the influence of participating insiders and ensuring that the IBC is appropriately advised.

Information

The Panel also considered the position around the equal access to information by bidders, although this time through the lens of insider participation in a bid. The position adopted by the Panel in GN19 was that where target directors do not provide equal access to information to a rival bidder where there are participating insiders, they should have a sound underlying reason for not doing so. However, such a position is likely to be heavily scrutinised by the Panel.

Disclosure to shareholders

GN 19 emphasises the importance (for both target and bidder) of providing sufficient information to target shareholders to allow them to assess the merits of the relevant transaction. In particular, the Panel is concerned to ensure that where a bid that has had the involvement of participating insiders, the relevant bidders should not enjoy an information advantage over target shareholders.

One particular issue considered by the Panel was the provision of management forecasts (covering future financial, operational and other performance of the business) to bidders and the fact that such information was not typically provided to target shareholders. The Panel also identifies whether a target board should be required to reconcile providing management forecasts to bidders (with insider participation), with a decision to not disclose them to target shareholders.

Other policy issues canvassed by the Panel

The Panel also identified other potential issues of concern which may arise in private equity/insider bids (but noting, that they did not consider that these issues needed to be covered in GN19).

Anti-competitive practices

Actions which may reduce competition in the market for control, including via curtailing the availability of advisors to rival bidders and actions and conduct between bidders which reduces competition for a target company. The Panel formed the view that such considerations were thought of as outside of the scope of the Panel's paper and in any event, these concerns applied equally to all bids, not just those involving participating insiders.

Independent experts

In comparing the treatment of insider bids in the US and UK, the Panel pondered the requirement for preparation of independent expert reports where participating insiders where involved. Ultimately, the Panel formed the view that it is the role of target directors to determine whether or not commissioning an independent expert report will assist target shareholders in their assessment of the bid.

Other issues

Reflecting the media reporting of the period, the Panel's issues paper also considered more general 'issues' potentially arising from private equity bids outside of immediate concerns around insider participation. At the time, the Panel noted that these issues would normally fall outside its jurisdiction or interest, and were not relevant to the work of the Panel.

These issues included:

- a concern that the structure of private equity bids may mean an increased risk of insider trading (the Panel's thinking was that reliance on a greater number of lenders and longer diligence periods (as a result of higher gearing) could exacerbate the risk of insider trading)
- the implication of higher gearing levels of financing for funding and disclosure for stub equity
- regulatory concerns surrounding private equity, namely foreign investment and competition law

Clayton James is an M&A Partner of Herbert Smith Freehills.

Andrew Rich and Joshua Santilli

Navigating jurisdictional turf: the evolving role of the Takeovers Panel in schemes of arrangement

Since the Takeovers Panel emerged in its revitalised form on 13 March 2000, it has made a vast and valuable contribution to the general regulatory framework and development of market practice applicable to control transactions involving widely-held Australian companies.

In the case of takeover bids, this has been facilitated by the general statutory prohibition against the commencement of court proceedings relating to takeover bids before the end of the bid period, which has had the intended effect of making the Panel the main forum for resolving takeover disputes.

In contrast, the scope of the Panel's role in relation to control transactions effected by way of a scheme of arrangement, and the outer limits of its jurisdiction in relation to such matters, is less clear. The provisions in the *Corporations Act 2001* (Cth) (Corporations Act) that outline the scope of the Panel's general jurisdiction, which is linked to the broad concept of 'unacceptable circumstances', make no specific reference to schemes of arrangement, nor do the provisions of Part 5.1 of the Act relating to schemes of arrangement make any specific reference to the Panel.

In the absence of clear legislative guidance, the Panel has had to carefully consider for itself the question of if and when it will be appropriate for it to conduct proceedings relating to schemes of arrangement. Similarly, in matters concerning both takeovers and schemes, the courts have had to grapple with the question of how they ought to go about exercising their jurisdiction over subject matter shared with the Panel.

In this article, we trace how the Panel's understanding of its jurisdiction in matters involving schemes of arrangement has evolved over time, and provide an overview of the significant contributions it has made in this area.

Early days and general principles

St Barbara Mines

In October 2000, the Panel was forced to confront the question of if and when it would be appropriate for it to involve itself in a matter concerning a change of control resulting from a scheme of arrangement. The question arose following an application by shareholders in St Barbara Mines Limited for a declaration of unacceptable circumstances in relation to the proposed merger of St Barbara with Taipan Resources NL, which was to be effected by parallel members' and optionholders' schemes of arrangement. The aggrieved shareholders sought a wide variety of interim and final orders, alleging (among other things) that the structure of the proposed merger was not compliant with the Corporations Law (as the legislation was then known) and that the disclosure in the explanatory statement dispatched to shareholders was also non-compliant. The Panel declined to conduct proceedings and, in explaining its reasons for doing so, set out a number of general principles which have been applied in a significant number of subsequent Panel decisions since. The general principles were:

- despite there being no express exclusion of members' schemes of arrangement from the Panel's power to declare unacceptable circumstances, it will generally be inappropriate for the Panel to conduct proceedings concerning a scheme of arrangement
- the wide discretion bestowed on courts under the scheme provisions is evidence of a legislative intention that they be the primary forum for the resolution of issues relating to schemes – accordingly, the Panel will generally be reluctant to initiate proceedings where a court has already commenced scrutiny of a scheme
- there may be exceptional cases in which the Panel's functions complement rather than interfere with those of the court

Applying these principles, the Panel reasoned that providing the relief requested by the applicant shareholders in St Barbara Mines would involve intervention in court-ordered scheme meetings, as well as the court-supervised aspects of the scheme process, and that this was not an 'exceptional case' where the Panel's functions would complement those functions; accordingly, the Panel declined to conduct proceedings.

The Taipan angle

A separate Panel application was made soon after the St Barbara Mines decision by Troy Resources NL (Troy). Troy had launched a takeover bid for Taipan Resources NL (the proposed acquirer of St Barbara Mines under the scheme discussed above). Its application to the Panel impugned the conduct of Taipan in relation to the proposed merger with St Barbara, including in relation to certain Taipan shareholder approvals that were

Andrew Rich and Joshua Santilli

Navigating jurisdictional turf: the evolving role of the Takeovers Panel in schemes of arrangement

required in connection with that merger. The day following its application to the Panel, Troy commenced proceedings in the Supreme Court of Western Australia alleging oppressive conduct on the part of Taipan (stemming from the same conduct it sought to impugn in its Panel application). Extending the reasoning adopted in the St Barbara Mines decision, the Panel noted that:

- it will generally be inappropriate for the Panel to conduct proceedings in relation to an application where the evidence and the issues to be considered by the Panel are already before the court
- the Panel will be keen to avoid duplicative proceedings and discourage forum shopping in circumstances where the functions of the court and the Panel overlap

In light of the substantial overlap between Troy's pending oppression application in the Supreme Court of Western Australia and its application to the Panel, the Panel determined that it would be impossible to effectively separate the issues in Troy's oppression application from those that might be considered by the Panel, and declined to conduct proceedings.

Applying and developing the general principles

The St Barbara Mines and Taipan Resources decisions established the general criteria against which the Panel has come to test whether it is appropriate for it to conduct proceedings in matters involving schemes of arrangement. Over time, through the nuanced application of those principles, the Panel has made a significant contribution to the regulatory framework applicable to schemes, including in relation to exclusivity arrangements, break fees, market disclosures made ahead of the first court hearing, the application of ASIC's 'truth in takeovers' policy, and the regulation of trust schemes. These contributions are discussed in further detail below.

Panel scrutiny of exclusivity arrangements in the scheme context

The area in which the Panel has perhaps been most willing to conduct proceedings in the scheme context is that relating to exclusivity arrangements and other deal protection devices (including break fees). This makes eminent sense in that:

- generally speaking, exclusivity arrangements are announced some weeks (or months) before a target initiates court proceedings in relation to a proposed scheme – accordingly, there is a relatively lengthy period in which no court has 'commenced its scrutiny of the scheme' in the St Barbara Mines sense
- the Panel's distinct ability as an administrative body to create new rights and obligations provides it with the unique ability, complementary to the courts' separate function of determining existing legal rights and obligations, to vary and reshape exclusivity regimes agreed between targets and bidders so as to ensure that control transactions effected by schemes take place in a maximally efficient, competitive and informed market

National Can Industries

A useful practical illustration of this is the Panel's decision in National Can Industries Ltd (No 1) & National Can Industries (No 1R) (2003) 48 ACSR 409. In that decision, the Panel determined that a break fee provided for under the terms of a scheme implementation agreement between National Can Industries (NCI) and the proposed bidder, ESK, was unacceptable (ESK being a company whose sole shareholder and director was the managing director of NCI itself – the managing director's family also held a controlling stake in NCI). The unacceptability of the break fee resulted from, among other things, the related party nature of the transaction, the lack of urgency for the ESK proposal, and NCI having agreed to potentially pay the break fee before its independent directors had received the independent expert's report. The unacceptable circumstances arose prior to NCI and ESK entering into a second implementation agreement providing for a higher offer price.

The unique ability of the Panel to vary exclusivity arrangements (or, in this case, the effect of those arrangements) was evidenced by its creative solution to resolve the break fee issue by way of undertakings from ESK to:

- increase the scheme consideration payable under the second scheme by an amount by which the payment of the first break fee depleted the assets of NCI on a per share basis (therefore ensuring that shareholders were not adversely affected by the payment of the first break fee if they approved the second scheme)

- repay the first break fee if a rival bid was announced before the second scheme meeting and was eventually successful (therefore ensuring that if a rival bid succeeded, NCI's assets would not have been depleted by the payment of the first break fee, overcoming any adverse effect of the fee on the rival bid)

The review Panel ultimately decided not to vary or set aside this decision of the initial Panel, and the second scheme was subsequently approved by shareholders and the Court.

Other cases

Similarly in Ross Human Directions the Panel determined that certain deal protection measures in the scheme implementation agreement at issue in those proceedings would have an unacceptable effect on competition for control of the target company – again, the Panel was able to efficiently resolve that issue by way of undertakings to amend the scheme implementation agreement to, among other things, incorporate various qualifications to the 'no due diligence', 'no shop' and 'fiduciary exception' provisions.

More recently, in Re GBST Holdings Limited, the Panel scrutinised, in the context of a multi-bidder auction for control, a process and exclusivity deed which was entered into by the target, GBST, with a view to subsequently executing a scheme implementation agreement giving effect to one bidder's non-binding indicative proposal. The terms of the process deed were summarised and announced to the market shortly after its execution. While the Panel ultimately determined that the process adopted by GBST, and its entry into the proceed deed itself (as well as its terms), were not unacceptable, it did cause GBST to release a complete copy of the process deed to the market, subject to some redactions of certain commercially-sensitive information unrelated to the exclusivity provisions.

The Panel's role in promoting fulsome disclosure in transactions effected by way of a scheme of arrangement is discussed further below.

Disclosure in schemes

Content in the scheme booklet

One area in which the Panel has very sensibly declined to exercise its jurisdiction in the schemes context is in matters concerning challenges to the adequacy of disclosure made in the explanatory statement or 'scheme booklet' dispatched to target shareholders.

The Panel's position in this regard is readily understandable, particularly considering that:

- the discretionary power to approve the explanatory statement is expressly conferred on the court
- the Corporations Act also provides for ASIC to be provided with 14 days' notice of the hearing of the application to convene the scheme meeting (and therefore, in practice, a 14 day period to review the disclosures made in the draft explanatory statement)

In light of that statutory framework, and given the desirability of avoiding duplicative proceedings, the Panel will 'generally not look to second guess the court in relation to documents that it has approved or considered'.

Ancillary disclosure documents not considered by the court

This is to be contrasted with disclosure documents which are related to the scheme transaction but which the court is not strictly required to consider; for example, in the complex Anaconda Nickel proceedings, the Panel noted that it would be showing 'no disrespect to the [Supreme Court of Western Australia] to order further disclosure' in relation to a rights issue prospectus prepared following the Court's approval of related creditors' schemes of arrangement, as the Court, in approving the schemes, had not been required to, nor did it, consider the adequacy of disclosure in the rights issue prospectus.

Disclosures before the first court hearing

In contrast to the case of disclosures made in the scheme booklet, the Panel has had a significant role to play in scrutinising market announcements concerning scheme transactions which are made prior to the first court hearing. Typically these announcements concern exclusivity arrangements, or the execution of a scheme implementation agreement. At this early stage in the transaction timeline the court has not yet 'commenced scrutiny' of the scheme and, on that basis, it is entirely appropriate for the Panel to intervene and, if necessary, order supplementary disclosure to ensure that the market is fully informed (assuming the announcement is inaccurate, incomplete or misleading).

Relatedly, there is no statutory requirement for a target company to release a full copy of the scheme implementation agreement when it announces a transaction to be effected by way of a scheme of arrangement. However, in no small part due to the

Panel's exercise of jurisdiction in this area, it has become standard market practice to do so. Indeed, the trend toward more fulsome disclosure (as opposed to, for example, a summary of the key terms of the scheme implementation agreement) was largely precipitated by the Panel's decision in Re BC Iron Ltd. In that case, the announcements dealing with the proposed acquisition of BC Iron by Regent Pacific Group Ltd made no mention of the fact that clause 15.1(d) of the scheme implementation agreement provided Regent Pacific with a termination right if the Regent Pacific Board publicly changed or withdrew its recommendation – subsequently, Regent Pacific purported to terminate the agreement on the basis of that termination right.

The Panel did not hesitate to declare unacceptable circumstances and order that Regent Pacific could not rely on clause 15.1(d) of the scheme implementation agreement to terminate it. The Panel stated the general principle as follows:

> **When a scheme proposal is announced, the parties to the proposal should ensure that the announcement is either accompanied by a copy of the scheme implementation agreement or includes a summary of those provisions of the agreement necessary to ensure that, when the full agreement is published (usually in the scheme booklet), the market does not become aware that the proposal is in fact less favourable than was announced. This would include dealing in the announcement with matters such as conditions, termination rights, exclusivity provisions and break fees. Such disclosure is necessary to ensure that there is an efficient, competitive and informed market for the acquisition of control over shares in the target following the announcement.**

The Panel has adopted similar reasoning in the case of agreements executed prior to, but in anticipation of ultimately entering into, a scheme implementation agreement – this has, in certain cases, resulted in parties disclosing full copies of heads of agreement or process deeds relating to proposed scheme transactions, particularly where summaries of the key terms of those documents have been alleged to be inaccurate or otherwise incomplete.

Truth in takeovers: application to schemes

Another significant area in which the Panel found it appropriate to exercise its jurisdiction in the scheme of arrangement context is in applying ASIC's 'truth in takeovers' policy. Under that policy, ASIC states that it will hold substantial holders of target shares to the course of action contained in public statements of intention made by them.

The truth in takeovers policy itself makes no reference to schemes of arrangement, rather it is expressed in the language of 'bidders' and 'takeover bids' – for this reason, there was previously a lack of clarity as to whether the truth in takeovers policy would apply in relation to public statements of intention made in the context of a control transaction proposed to be effected by a scheme of arrangement. This issue was ultimately put to rest by the Panel in its decision in Re Ludowici Limited, involving a 'no increase' statement made by a proposed acquirer which went uncorrected for some time – an interloper emerging with an alternative scheme proposal at a higher price argued that the proposed acquirer ought to be held to its no increase statement.

The Panel rejected a submission that as both proposals involved schemes of arrangement it should decline to conduct proceedings (noting that the Court had not yet 'commenced scrutiny' of the schemes) and held that ASIC's truth in takeovers policy should apply in the scheme context, despite the fact that the policy does not expressly apply to schemes. The Panel proceeded to made orders providing for compensation to those target shareholders who had sold their shares on market in reliance on the no increase statement (as opposed to holding the proposed acquirer to its 'no increase' statement).

Even if a court has commenced scrutiny of a scheme of arrangement, the Panel's broad power to make any order that it thinks appropriate, if it has made a declaration of 'unacceptable circumstances', may (depending on the circumstances) mean that the Panel is better placed than the court to address departures from, and to enforce, the 'truth in takeovers' policy.

The novel case of trust schemes

A distinct area in which the Panel has assumed a broader jurisdiction in the case of schemes of arrangement is in the regulation of trust schemes.

No provisions in the Corporations Act specifically regulate trust schemes. Whilst it is 'commonplace' for judicial advice to be sought from the court under the applicable trustee legislation that the trustee (or responsible entity) of the relevant trust would be justified in taking some or all of the steps required to give effect to the proposed trust scheme, this is not strictly required. If judicial advice is sought it is typically sought at two stages (before meetings have been convened and after securityholder approval has been obtained) and likewise courts proceed by analogy with the approach they take in members' schemes of arrangement.

In light of the various parallels with members' schemes of arrangement, one might expect the Panel to have had a very limited role to play in the case of trust schemes – however, this has not been the case, the key distinction being that the Corporations Act does not (unlike in the case of members' schemes of arrangement) expressly bestow a discretion on the part of the courts to 'approve' trust schemes.

The Panel was brought into the realm of the regulation of trust schemes by the application of Mirvac Funds Limited for a declaration of unacceptable circumstances in respect of a complicated merger proposal involving the responsible entities of the Commonwealth Property Office Fund (CPA) and Gandel Retail Trust (Gandel) for CPA and Gandel to merge the four funds which made up the Colonial First State Property Trust Group with CPA and Gandel. The application covered a range of matters and also included the referral by the Takeovers Panel to the Federal Court of Australia of several questions of law.

Once the threshold question of the legitimacy of the trust scheme had been answered in the affirmative, a key issue for the Takeovers Panel was whether certain Commonwealth Bank Group entities could vote on the proposal. While the Panel has typically been reluctant to intervene in matters concerning voting on members' schemes of arrangement, in light of the factors discussed above this is not the case in matters involving trust schemes. Ultimately the Panel determined that, subject to the receipt of certain undertakings, the entities should not be excluded from voting.

In consequence of the Colonial First State matter, the rise of the use of trust schemes, and in particular the absence of any provisions in the Corporations Act specifically regulating trust schemes, the Panel sought to fill the regulatory void through the release of Guidance Note 15, titled 'Trust Scheme Mergers'. The Guidance Note emphasises the close analogy between trust schemes and schemes of arrangement and requires certain procedures and other matters (drawn from the scheme of arrangement and takeover bid provisions in the Corporations Act) to be observed by those embarking on a trust scheme, including equality of opportunity principles, comprehensive disclosure to shareholders, the inclusion of an independent expert report and so forth. This significant contribution from the Panel undoubtedly helped facilitate the many dozens of trust scheme mergers in the years that followed.

By way of contrast with the position in relation to members' schemes of arrangement, the Panel has also shown a willingness to involve itself in challenges to the adequacy of disclosure in relation to trust schemes, even if judicial advice proceedings have been commenced. In the case of Re Investa Office Fund, the Panel made orders for (among other things) supplementary disclosure to remedy deficiencies in a document issued by the holding company of Investa Office Fund's (IOF) responsible entity and manager, IOMH. That document encouraged IOF unitholders to vote against a proposal by DEXUS Property Group to acquire the interests in IOF, but failed to readily and reasonably disclose the interests of IOMH in advocating its position that IOF unit holders vote against the DEXUS proposal (including the fact that it stood to lose significant fees if the DEXUS proposal was approved and implemented).

Andrew Rich and Joshua Santilli

Navigating jurisdictional turf: the evolving role of the Takeovers Panel in schemes of arrangement

In the same proceedings, a challenge was also raised by DEXUS to the entitlement of a Morgan Stanley entity to vote IOF units held by it on the DEXUS proposal, by virtue of an alleged association with the responsible entity (IOMH) and the application of section 253E of the Corporations Act (which prohibits a responsible entity of a registered scheme and its associates from voting on a resolution at a meeting of the scheme's members if they have an interest in the resolution other than as a member).

The Panel ultimately declined to interfere with the voting rights attaching those units, noting in the course of its reasoning that consent orders had been made by the New South Wales Supreme Court declaring that the relevant entity was not precluded from voting by reason of section 253E. The Panel did, however, leave open the possibility that it may make orders with respect to voting rights in a trust scheme matter in appropriate circumstances:

> **Morgan Stanley submitted that 'the appropriate forum for determination of the Voting Issue is the Court.' We do not agree entirely. In forming our conclusion we have not abdicated our responsibility by merely deferring to the Court. The Panel jurisdiction to declare unacceptable circumstances is a broad, policy–based jurisdiction; Courts and the Panel may each exercise a different jurisdiction over the same subject matter. It is undesirable to place the jurisdictions in potential conflict, and we have therefore paid particular attention to the findings of the Court, but we have decided the issues before us for ourselves.**

> Recent decisions show that the Panel will still intervene where it has concerns with the rights issue process, particularly where the Panel believes there may be a control purpose.

Conclusion

Despite early indications that the Panel might decline to exercise jurisdiction in scheme of arrangement matters, other than in 'exceptional cases', the Panel has made substantial contributions in this space, and has significantly shaped the regulatory landscape relating to (among other matters):

- exclusivity arrangements
- market disclosure (including the application of the 'truth in takeovers' policy)
- the regulation of trust schemes

In the Panel's **2015 stakeholder survey, 82%** of respondents noted their preference to seek resolution by the Panel in matters where the Panel's jurisdiction is shared with the courts

Indeed, in the Panel's 2015 stakeholder survey, 82% of respondents noted their preference to seek resolution by the Panel in matters where the Panel's jurisdiction is shared with the courts. In light of that highly positive feedback from market participants and their advisors, it is not unreasonable to expect that we will continue to see the Panel's role in scheme of arrangement matters further evolve and expand in the future, as it continues to exercise jurisdiction in this area.

Andrew Rich is an M&A Partner of Herbert Smith Freehills. He is a co-author of Schemes, Takeover and Himalayan Peaks, a leading book on public company mergers.

Joshua Santilli is a Solicitor at Herbert Smith Freehills.

Caroline Rae and Antonia Kirkby

Postcard from London

The UK Takeover Panel is arguably the most well known of all takeover regulators, principally because it was the first of its kind. Following its establishment in 1968, many jurisdictions across Europe and Asia introduced regimes based on the UK model. Australia adopted a different approach. Whilst the Australian Panel focuses on hearing applications made before it based on Australian takeover legislation, the UK Takeover Panel plays a proactive role in supervising and regulating takeovers.

This means that the day to day functions of the UK Takeover Panel are different to that of the Australian Panel. However, the spirit and aims of the two regimes are similar – both have fair treatment of shareholders as a central objective, the general principles underpinning the regulatory frameworks are consistent and the way takeovers are structured by way of takeover offer or by scheme look familiar.

That said, each regime has of course evolved in its own way to tackle the issues that arise in the particular jurisdiction. The UK regime has undergone significant reform, particularly during the last decade, and as a result there are some significant differences which impact how takeovers are effected.

Caroline Rae and Antonia Kirkby
Postcard from London

How the UK Takeover Panel operates

Takeovers and mergers in the UK are governed by The City Code on Takeovers and Mergers (the Code), which applies whenever there is an acquisition or consolidation of control. The Code is written and administered by the UK Takeover Panel.

Day to day decisions as to enforcement and interpretation of the Panel Rules are made by the Panel Executive (which is a full-time body composed largely of secondees from various City institutions).

The Code is not written in a legalistic style and it is the spirit rather than the letter of the Code which must be observed. For this reason, the Panel Executive is available at short notice to give guidance or rulings on matters arising under the Code and must be consulted whenever there is any doubt as to the application of the General Principles or Rules of the Code.

If a party is unhappy with a ruling by the Panel Executive, it may appeal to the Hearings Committee of the Takeover Panel. However, it is fairly rare for the Hearings Committee to be convened. In the year to July 2019, according to the Panel's annual report, it met to consider the price at which the Walt Disney Company should be required to make an offer for Sky under the 'chain principle'; and later that year the chairman refused a request from Mr David King for the Committee to be convened to review a ruling of the Panel Executive. The chain principle involves a situation where a bidder acquiring an interest resulting in over 50% of the voting rights in a target company will, as a result, acquire control of a second company for which the target company holds a controlling block of shares. The bidder, in some instances, will be required by the Panel to make an offer for the second company.

Decisions by the Hearings Committee can be appealed to the Takeover Appeal Board. Takeover Appeal Board hearings are also rare, with the most recent rulings again relating to the chain principle offer for Sky plc in 2018 and an appeal by David King in relation to the Panel ruling that he must make a mandatory bid for Rangers International Football Club in 2017.

The decisions by the Hearings Committee and Takeover Appeal Board typically support the Panel Executive's original ruling.

Panel's role on a bid

The Panel Executive is an 'active' regulator and frequent contact between the Panel Executive and the advisers to the Bidder and Target is common in UK takeovers. The Code makes clear that taking legal advice on the interpretation or application of the Code is not an appropriate alternative to obtaining a ruling from the Executive. In some instances, consultation with the Panel is required by the rules of the Code.

It expects parties to deal with it in an open and cooperative manner and, in one concert party investigation, the parties were sanctioned for failing to deal openly with the Panel, even though the investigation concluded there had not in fact been a breach of the concert party rules.

Advisers (both financial advisers and legal advisers) have been publicly criticised by the Panel for not taking all reasonable care to ensure that the commercial background and the purpose of a transaction was fairly presented to the Panel and that the Panel was provided with all of the facts in their respective possession regarding connections between the parties.

Whilst possibly the most contentious area for the Panel is concert party issues, it can and does issue rulings (privately) in a wide range of situations. Examples of situations where rulings may be made include where parties make statements which are not substantiated (for example about levels of shareholder support) or have to be clarified (because they have suggested that a bid will not be increased without making a formal 'no increase' statement).

Even before a bid is announced, the Panel will be monitoring for price movement and/or speculation in the market and determining whether a leak announcement is required.

The role of the courts

Litigation in the context of takeovers is extremely rare in the UK, as the courts are reluctant to intervene. The most notable case on this point is R v Panel on Takeovers and Mergers ex parte Datafin. In that case, Datafin sought to challenge, by way of judicial review, a Panel ruling in the courts. The Court of Appeal held that decisions of the Panel are susceptible to judicial review by the courts but that the courts would generally accept the Panel's interpretation of the Code and would be unlikely to intervene. The courts will also only intervene in retrospect, not in the course of a live transaction.

Even on a takeover by way of scheme, which involves a court process, the courts will be reluctant to intervene. In the case of Expro International, shareholders asked the court to adjourn a decision to sanction the scheme implementing the takeover of Expro as there was a possibility of a higher competing offer. The judge rejected the application for adjournment saying that no criticism could be made of the board's assessment of the relative benefits and risks associated with accepting or rejecting the competing proposal and the shareholders had been told about the potentially competitive situation prior to the scheme meeting but had approved the scheme anyway. The scheme was duly sanctioned.

Panel sanctions

Sanctions for a breach of the Code rules generally involve a public or private censure. For the most egregious breaches the Panel may issue a 'cold-shoulder' ruling which means that no regulated entity, such as a financial adviser, may act for the sanctioned person on Takeover Code-related matters. Whilst these sanctions may seem relatively inconsequential, they are taken very seriously in the legal and financial adviser communities in the UK, with even a private censure being seen as a serious matter.

The most recent 'cold-shoulder' ruling was issued in respect of David King – and is only the third time the Panel has used this power.

Changes introduced by the UK Takeover Panel in recent years

When the UK Takeover Panel amends the Code, it is usually to address challenges faced on particular transactions. The most significant overhaul of the Code in recent years was in 2011 following the hostile and protracted bid for Cadbury by Kraft. When Cadbury eventually succumbed to the takeover, there was a widespread perception that the Code did not afford enough protection to targets and various measures were introduced to try and address this imbalance. Changes included:

- A prohibition on break fees and other deal protection measures
- The imposition of an automatic 28 day deadline for the bidder to clarify its intentions following a leak or possible offer announcement (referred to as 'put up or shut up' or 'PUSU'). By the end of the 28 day period, the bidder must either announce a firm intention to make an offer (which means, amongst other things, that the bidder must be in a position to pay in full any cash consideration under the offer) or announce that it does not intend to make an offer (and it will generally then not be allowed to make a bid for six months). The deadline can only be extended at the request of the target and the intention is to prevent a target being 'under siege' for too long
- A requirement that any statement of intention or belief on an offer must be both an accurate statement of the party's intention at the time it is made and made on reasonable grounds

Since then, the focus on intention statements has continued whilst a party making an intention statement is not legally bound to comply with it, after 12 months it will have to confirm whether it followed the stated course of action. A new regime has also been introduced to allow a party to an offer to elect to make binding commitments on particular issues, for example keeping the target headquarters in the UK. The giving of a post-offer undertaking (POU) is entirely voluntary but, if given, it is a legally binding commitment with which the giver must comply.

As we look ahead, and the UK leaves the EU, we expect the Panel to turn its attention to how it treats conditions relating to merger controls in the EU as compared with merger clearance elsewhere in the world. Currently, a bidder is able to invoke UK and EU merger control conditions more easily than those for other jurisdictions. It may also focus on conditions relating to national security clearance, as the UK is proposing a new foreign direct investment regime in the UK.

Caroline Rae and Antonia Kirkby

Postcard from London

For the most egregious breaches the Panel may issue a 'cold-shoulder' ruling which means that no regulated entity, such as a financial adviser, may act for the sanctioned person on Takeover Code-related matters. Whilst these sanctions may seem relatively inconsequential, they are taken very seriously in the legal and financial adviser communities in the UK, with even a private censure being seen as a serious matter.

The Panel also has power to issue compensation orders to compensate shareholders, restraining directions, reporting a party to another regulator (for example the Financial Conduct Authority, who could consider delisting an entity or revoking an adviser's authorisation under the financial services legislation, or the Department for Business, Energy and Industrial Strategy, who could declare that an individual is unfit to be a director of a public company).

Other sanctions are also available against any persons found guilty of market abuse, insider dealing, making false statements, engaging in false conduct in connection with a takeover or fraud.

Concluding thoughts

The Panel aims to be a proactive regulator that deals with and resolves issues during the course of the bid. To date, the Panel has been successful in avoiding policing matters after the event – as evidenced by the fact it has only gone to court once to have its rulings enforced. Overseas bidders are often surprised by the limited use of its sanction powers. However, its methods certainly appear to work. Even private criticism by the Panel of market participants is considered highly embarrassing in the City of London and so a party who is not willing to abide by the Panel's rules and rulings may find it difficult to find advisers. Whilst this form of regulation may seem anachronistic, it appears – so far at least – to be effective.

Caroline Rae is an M&A Partner of Herbert Smith Freehills in London.

Antonia Kirkby is a Senior Lawyer at Herbert Smith Freehills in London.

David King and Rangers International Football club

The most challenging case the Panel has faced in recent years involved Mr David King and acquisitions of shares by Mr King and his concert parties in Rangers International Football Club.

In brief, the breaches of the Code included the following:

- Mr King and his concert parties acquired more than 30% of the voting rights in Rangers without making a mandatory offer, as required by the Code This was despite having been reminded of the consequences of breaching the 30% threshold
- Even when the Panel ruled that Mr King should make a mandatory offer, he did not. Ultimately, the Panel had to obtain a court order compelling him to make the offer. This is the first time the Panel Executive has had to seek a court order to enforce one of its rulings
- The Panel then initiated proceedings for contempt of court when Mr King had not made the offer by the specified deadline.
- Mr King failed to consult the Panel about the concert party analysis at the outset, in breach of the Code
- Mr King provided incorrect and misleading answers to the Panel Executive during the course of its investigation, in breach of the Code
- Mr King failed to include a cash confirmation statement in the announcement of a mandatory offer when the offer was finally made. The Panel then obtained an order restraining Mr King from publishing an offer document without a cash confirmation statement as required by the Code

The case involved the Hearings Committee, the Takeover Appeal Board, court rulings to enforce the Panel's decision and ultimately ended in the Panel issuing a 'cold-shoulder' ruling in respect of Mr King which will last for four years.

Baden Furphy

Where to now for the Takeovers Panel?

The great success of the Takeovers Panel, and its overwhelming acceptance by market participants, means it would be easy for the Commonwealth Government and the Panel to carry on its current form, doing the same sort of things it currently does.

However, there have been significant developments in the law and practice relating to corporate control transactions since the Panel (in its current form) was established twenty years ago. Such examples include:

- changes in the dynamics of trading in listed securities, including the use of derivatives, stock borrowing and short selling
- the increasing prevalence of shareholder activism and related importance of environmental, social and governance considerations for companies and investors
- the greater general regulatory scrutiny that applies to company takeovers including by FIRB and the ACCC

There is no sign that the pace of change will slow.

Given these developments, it is time to consider possible changes to the functions of the Panel and the way it operates.

Schemes of arrangement

It is clear that the use of schemes of arrangement to effect change of control transactions has increased significantly in the last twenty years, especially in large scale transactions.

Takeovers and schemes of arrangement are now basically alternative ways to acquire control of a listed entity. Most bidders contemplating a friendly acquisition of a listed entity will prefer to proceed by way of scheme of arrangement, rather than takeover. The key advantages are the 'all or nothing' nature of a scheme (which will often be critical in debt financed private equity acquisitions, for example) and the potentially lower 75% threshold required to achieve 100% ownership of the target (compared to the 90% threshold for compulsory acquisition under a takeover).

One disadvantage of utilising the scheme process is the time, cost and sometimes the uncertainty associated with the court review process. Two court hearings are generally required for a scheme, being for approval to convene the shareholder meeting and, once all necessary shareholder approvals have been obtained, to approve the scheme itself. This comes at considerable expense. This raises the question of whether the courts are the most appropriate body to supervise schemes of arrangement, or whether there is a potential role to play for the Takeovers Panel.

The New Zealand scheme provisions are similar to the Australian provisions, and include a requirement for two court hearings. The panel must provide a no objection statement or the court must be satisfied that shareholders will not be adversely affected by the transaction not being undertaken by way of a takeover. This is similar to the role played by ASIC in relation to no objection statements in the Australia jurisdiction. In New Zealand, the panel also has responsibility for appointing the independent expert for both schemes and takeovers.

Granting the Panel a broadly similar role to that played by the courts in the context of the acquisition of listed entities undertaken by way of scheme of arrangement should be considered. The objectives of bringing a commercial, practical perspective to takeover disputes, and ensuring that takeover disputes are resolved quickly and efficiently, logically extend to the supervision of schemes of arrangement to effect change of control transactions.

The advantages of this approach include:

- ensuring that there is an alignment of views and approaches to the regulation of takeovers and schemes which, as noted above, have essentially become transaction alternatives
- It avoids the current overlap between the jurisdiction of the Panel to hear certain disputes regarding schemes and the jurisdiction of the courts in supervising schemes
- It would remove the ability for entities to 'forum shop' in respect of the court or judge to hear scheme of arrangement cases

The current role played by ASIC in relation to schemes, including the review of the scheme booklet and having the power to grant relief from the disclosure requirements in the Corporations Regulations, could continue.

Baden Furphy
Where to now for the Takeovers Panel

Streamlining operations

One of the great benefits of the approach of the Takeovers Panel is its relative lack of formality, the ease with which matters can brought to the Panel and the speed at which takeover disputes are resolved by the Panel.

However, this also represents a potential trap for the Panel. It gives rise to the risk of trivial matters consuming its resources and causing unnecessary distractions for shareholders.

There is no easy way to address this problem, but some possible approaches are outlined below

The Panel could consider making cost orders more frequently against parties who are unsuccessful in Panel proceedings

This has happened to some extent, but is not currently regarded as a real deterrent. The costs recoverable could include not only the costs incurred by the opposing party but costs incurred by the Panel itself.

This approach should be considered in particular where the participants in a takeover transaction bring a series of disputes, often on related matters, to the Panel (or seek reviews of Panel decisions concerning the same transaction).

Clarity as to the matters the Panel unwilling to consider

The Panel has, from time, stated that it will not conduct proceedings in certain matters. For example, disputes regarding board spills. Also, it now frequently decides not to conduct proceedings in relation to matters (although often submissions are made in connection with that decision and so there is a 'quasi' proceeding in any event).Collating these approaches and decisions into a single guidance note that provides some over-riding principles regarding when the Panel will commence proceedings, and the sorts of matters it regards as outside its jurisdiction would be a welcome development from many in the market.

Lifting the bar on declaring unacceptable circumstances in disclosure related disputes

There is often a tendency for the Panel to treat additional disclosure as the simplest and easiest way to address a problem. It provides the complaining party with a remedy but allows the bid to continue. The cumulative effect of these decisions, and the associated guidance, is more and more detailed disclosure documentation. This additional disclosure information is often impenetrable to retail investors and, paradoxically, provides greater scope for Panel applications to be made on the basis of inadequate disclosure.

In disclosure related disputes, the Panel should focus closely on whether the disclosure is likely to actually mislead shareholders, and whether the complaining party can address the claimed deficiencies through its own disclosures. The bar on requiring additional disclosure should be set high, especially where the complaining party is sophisticated and well-resourced, and can be assumed to be capable of protecting its own interests (and those of its shareholders).

Allowing the shareholders of small companies to contract out of the application of the Takeover laws

This would mean that companies with say a market capitalisation of less than A$10 million would not be subject to the takeover rules if shareholders approve that approach. The resulting benefit for the Panel is that it would no longer have to deal with takeover related disputes involving these small companies.

Increasing certainty for market participants

When the Takeovers Panel (in its current form) commenced twenty years ago, the power of the Panel to make a declaration of unacceptable circumstances even where no breach of the law occurred was a significant concern for lawyers practising in the takeovers area.

The concern was that the laws governing takeovers were expressed in such general terms that it would be impossible to predict the outcome of matters considered by the Panel, and therefore would create significant uncertainty in any Panel proceeding.

By and large, that concern has proven unfounded. The principles outlined in the Panel's reasons for decisions, and the guidelines published by the Panel, generally provide practitioners with clear guidance. The ability to engage in informal consultations with the Panel can also assist in particular cases.

Nevertheless, novel situations do arise from time to time on which it is very difficult to provide definitive guidance. Example of this include:

- How the minimum bid rule applies to pre bid stake building via swaps
- The scope of the Panel's '4 month lock out rule' (for example, its application to no extension or no waiver statements, or following a failed scheme)

In those types of situations, the Panel could be given a power to make an advance binding ruling on whether a proposed approach would give rise to unacceptable circumstances. A ruling would give the relevant party the confidence to proceed, or clarity that its proposed approach is not acceptable. This would reflect the approach taken by the UK takeovers panel.

A number of issues would need to be resolved if this approach was adopted, including:

- As parties would need to be able to seek a ruling from the Panel on a confidential basis, other relevant parties involved in the transaction would not always be able to make submissions. There is a question whether there is a role for ASIC in the process
- Are rulings issued by a sitting Panel or the Panel executive?
- What happens if the ruling is issued on the basis of incomplete or misleading information – presumably in that case, the ruling would not stand?

The three points outlined above represent a practitioner's view on what the future may hold for the Takeovers Panel. They are intended to generate discussion, acknowledging that detailed practical aspects of them require further consideration.

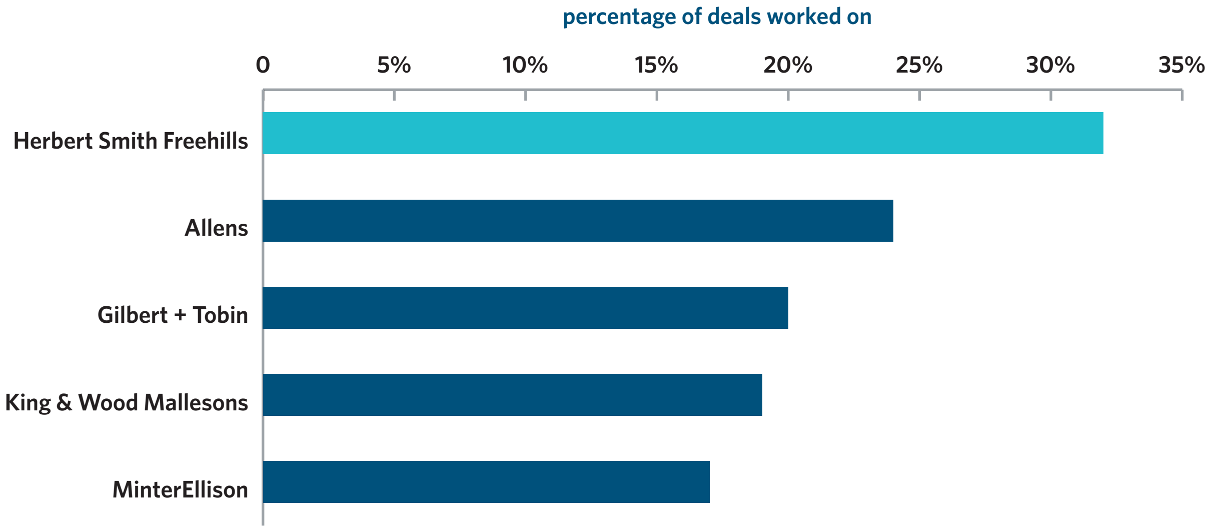
Baden Furphy is an M&A Partner of Herbert Smith Freehills.

About Herbert Smith Freehills

Herbert Smith Freehills is one of the world's leading global law firms, providing an integrated service across 27 offices. Operating as one global team, the firm uses innovative systems and processes to ensure our clients' work is delivered intelligently, efficiently and reliably. Herbert Smith Freehills is a market leader in takeovers, acting on some of the most complex and strategic takeovers and transactions in Australia and around the world. The volume and quality of transactions in which the firm is involved ensures that our clients have access to the deepest knowledge of market trends and latest issues.

ALL PUBLIC M&A DEALS > A$200 MILLION

1st July 2011 to 30 June 2019 Australian legal advisers acting for either the bidder or the target



The Herbert Smith Freehills team in Australia has recently advised:

- Wesfarmers on its A$19 billion demerger of Coles
- TPG Telecom on the proposed A$15 billion merger with Vodafone Hutchison by way of scheme
- Santos on its response to the A$14.4 billion approach from Harbour Energy
- Caltex Australia on its response to the A$10 billion (EV) Couche-Tard NBIO
- Amcor on its US$6.8 billion merger with Bemis Company Inc and redomiciliation to Jersey with an NYSE listing via scheme
- Healthscope on its A$4.4 billion acquisition by Brookfield by way of scheme

Authors

Tony Damian
Partner
T +61 2 9225 5784
M +61 405 223 705
tony.damian@hsf.com

George Durbridge
Special Advisor
T +61 3 9288 1424
george.durbridge@hsf.com

Baden Furphy
Partner
T +61 3 9288 1399
M +61 417 526 585
baden.furphy@hsf.com

Clayton James
Partner
T +61 2 9322 4337
M +61 447 392 896
clayton.james@hsf.com

Antonia Kirkby
Senior Lawyer
T +44 20 7466 2700
antonia.kirkby@hsf.com

Rodd Levy
Partner
T +61 3 9288 1518
M +61 417 053 177
rodd.levy@hsf.com

Rebecca Maslen-Stannage
Partner
T +61 2 9225 5500
M +61 419 767 709
rebecca.maslen-stannage@hsf.com

Caroline Rae
Partner
T +44 20 7466 2916
caroline.rae@hsf.com

Andrew Rich
Partner
T +61 2 9225 5707
M +61 407 538 761
andrew.rich@hsf.com

Joshua Santilli
Solicitor
T +61 2 9322 4382
joshua.santilli@hsf.com

Philippa Stone
Partner
T +61 2 9225 5303
M +61 416 225 576
philippa.stone@hsf.com

Notes

For a full list of our global offices visit **HERBERTSMITHFREEHILLS.COM**