



**ASIC**

Australian Securities & Investments Commission

## REGULATORY GUIDE 71

# Downstream acquisitions

May 2012

### About this guide

This guide is for companies, listed managed investment schemes, investors and their advisers who are involved in, or affected by, downstream acquisitions.

In some circumstances, a downstream acquisition may breach s606 of the *Corporations Act 2001* (Corporations Act).

This guide explains:

- the downstream acquisition exemption in item 14 of s611 (item 14);
- when we may grant relief;
- the conditions that may apply to our relief; and
- how to apply for relief.

### About ASIC regulatory documents

In administering legislation ASIC issues the following types of regulatory documents.

**Consultation papers:** seek feedback from stakeholders on matters ASIC is considering, such as proposed relief or proposed regulatory guidance.

**Regulatory guides:** give guidance to regulated entities by:

- explaining when and how ASIC will exercise specific powers under legislation (primarily the Corporations Act)
- explaining how ASIC interprets the law
- describing the principles underlying ASIC's approach
- giving practical guidance (e.g. describing the steps of a process such as applying for a licence or giving practical examples of how regulated entities may decide to meet their obligations).

**Information sheets:** provide concise guidance on a specific process or compliance issue or an overview of detailed guidance.

**Reports:** describe ASIC compliance or relief activity or the results of a research project.

### Document history

This version was issued in May 2012 and is based on legislation and regulations as at the date of issue.

Previous versions:

- Superseded Policy Statement 71, issued 15 November 1993, reissued 1 July 1996, rebadged as a regulatory guide 5 July 2007.

### Disclaimer

This guide does not constitute legal advice. We encourage you to seek your own professional advice to find out how the Corporations Act and other applicable laws apply to you, as it is your responsibility to determine your obligations.

Examples in this guide are purely for illustration; they are not exhaustive and are not intended to impose or imply particular rules or requirements.

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## A Overview

### Key points

A person may acquire a relevant interest in the shares of a downstream company as a result of an acquisition of a relevant interest in an upstream entity.

This guide explains:

- downstream acquisitions and when a person may breach s606 as a result of an upstream acquisition (see RG 71.1–RG 71.4);
- the exemption for downstream acquisitions in item 14 of s611 (item 14), our approach, the scope of the exemption, and when we may apply to the Takeovers Panel for a declaration of unacceptable circumstances even though the exemption in item 14 is satisfied (see Section B);
- when we may grant relief to allow downstream acquisitions that would breach s606 because they do not satisfy the exemption in item 14 (see Section C);
- the conditions that may apply to our relief (see Section D); and
- how to apply for relief (see Section E).

### What is a downstream acquisition?

RG 71.1 A downstream acquisition occurs when a person acquires a relevant interest in the shares of a downstream company as a result of an acquisition in an upstream entity (downstream acquisition).

RG 71.2 This is because a person is deemed under s608(3) of the *Corporations Act 2001* (Corporations Act) to have the same relevant interests in securities that an upstream entity has if they have voting power above 20% in, or control, the entity.

Note: For ease of reference, we have generally used the term ‘company’ and ‘shares’ when referring to the downstream company because this is consistent with the language adopted in Ch 6. However, Ch 6 and this guide also applies to the acquisition of relevant interests in voting securities of listed bodies and voting interests of listed managed investment schemes: s603 and 604. In relation to the upstream company, body or scheme, Ch 6 uses the terms ‘listed company’ and ‘body corporate’. For ease of reference, we have used the term ‘upstream entity’ throughout this guide.

RG 71.3 The downstream acquisition will breach s606 in circumstances where the relevant interest in the downstream company exceeds the thresholds in s606, unless an exemption in s611 applies. Item 14 of s611 (item 14) provides an exemption for certain downstream acquisitions.

RG 71.4 Two examples of downstream acquisitions that may breach the thresholds in s606 are set out below.

#### Example 1: Acquiring a relevant interest in an upstream entity

Company A acquires a relevant interest in 40% of the securities in Entity B where Entity B has a relevant interest in 25% of the shares in Company C. This will result in Company A acquiring a relevant interest in 25% of the shares in Company C (by the application of s608(3)(a)).

#### Example 2: Acquiring control of an upstream managed investment scheme

Company A acquires control of Scheme 1 where Scheme 1 has a relevant interest in 25% of the interests in Scheme 2 (a listed managed investment scheme). This will result in Company A acquiring a relevant interest in 25% of the interests in Scheme 2 (by application of s608(3)(b)).

Note: It is assumed in each example that Company A did not have an existing relevant interest in the shares in Company C or in the interests in Scheme 2.

## Purposes of Ch 6

RG 71.5 The purposes of Ch 6 as set out in s602 are relevant to downstream acquisitions. This is because a downstream acquisition may result in:

- (a) an upstream acquirer obtaining control over a substantial interest in the downstream company without downstream shareholders being given an opportunity to consider the proposal, contrary to the principle in s602(b); or
- (b) the downstream holders not being given an equal opportunity to share in any premium for control of the downstream shares that is reflected in the price paid for the upstream acquisition, contrary to the principle in s602(c).

RG 71.6 A downstream acquisition that satisfies the exemption in item 14 may nonetheless give rise to unacceptable circumstances if the acquisition offends the principles in s602. We will also consider the purposes of Ch 6 when considering whether to give relief to a downstream acquisition that does not satisfy the exemption in item 14 and the conditions that should apply to our relief.

## The exemption in item 14

- RG 71.7 The exemption in item 14 applies where the upstream entity is included in the official list of a prescribed financial market (such as ASX) or a foreign body conducting a financial market approved by us. ASIC's list of approved foreign exchanges is set out in Class Order [CO 02/259] *Downstream acquisitions: foreign stock markets*.
- RG 71.8 When considering whether a downstream acquisition is exempt from the prohibition in s606, persons acquiring a relevant interest in an upstream entity should be aware that there are limits to the scope of the exemption in item 14, and a downstream acquisition may risk an application to the Takeovers Panel for a declaration of unacceptable circumstances even though the exemption applies. For a discussion of the downstream acquisition exemption in item 14 and the circumstances in which it should apply, see Section B.

## When ASIC may grant relief

- RG 71.9 ASIC has discretionary powers under s655A to grant relief from the requirements of Ch 6. The circumstances where we may grant case-by-case relief to permit a downstream acquisition that does not satisfy the exemption in item 14 are discussed in Section C. ASIC will continue to monitor downstream acquisition transactions and consider new developments in this area, as appropriate.

## Conditions of relief that may apply

- RG 71.10 The types of conditions that we may impose on any relief we grant will depend on the circumstances of the downstream acquisition: see Section D. Table 1 in Section D summarises when certain conditions will apply and where to find more information on them.

## Applying for relief

- RG 71.11 Applications for relief should be made before the upstream acquisition is made. For details on how to apply for relief, see Section E.

## B The exemption in item 14

### Key points

Item 14 provides an exemption from s606 for downstream acquisitions where the upstream entity is listed on a prescribed financial market (including ASX) or on an approved foreign exchange.

This section explains:

- the exemption in item 14 (see RG 71.12–RG 71.15);
- our approach to the exemption (see RG 71.16–RG 71.18); and
- the scope of the exemption, including when we may apply to the Takeovers Panel for a declaration of unacceptable circumstances (see RG 71.19–RG 71.25 and RG 71.27–RG 71.29).

### The exemption in item 14

- RG 71.12 Item 14 exempts a downstream acquisition from breaching s606 where the acquisition results from an upstream acquisition of a relevant interest in voting shares of a body corporate that is included in the official list of:
- a prescribed financial market (including ASX); or
  - a foreign body conducting a financial market that is a body approved in writing by us.

- RG 71.13 The exemption in item 14 was introduced following a period of uncertainty in the law and recommendations by the Legal Committee of Companies and Securities Advisory Committee (CASAC) in its paper *Anomalies in the takeover provisions of the Corporations Law* (March 1994).

- RG 71.14 We have approved a list of foreign exchanges for the purposes of item 14: see [CO 02/259]. All of the foreign bodies conducting a financial market included in this list are also included in the list of approved foreign exchanges in Regulatory Guide 72 *Foreign securities prospectus relief* (RG 72).

Note: Unless otherwise stated, our relief only extends to the main board of these markets.

- RG 71.15 In approving the list of foreign exchanges included in [CO 02/259], we took into account the criteria set out at RG 72.54 because we consider that the extension of the item 14 exemption to foreign exchanges that meet these criteria satisfies the policy behind the exemption in item 14: see RG 71.17.

## Our approach to the exemption

RG 71.16 Our approach to the exemption for downstream acquisitions in item 14 is to uphold the policy behind the exemption while also taking into account the investor protections afforded to downstream shareholders in s602.

RG 71.17 The policy behind the exemption in item 14 is designed to:

- (a) preserve the free flow of shares in widely-held entities listed on appropriate exchanges;
- (b) prevent companies constructing a takeover defence through the acquisition of strategic parcels in downstream companies; and
- (c) enhance international comity through the removal of obstacles to primarily foreign business transactions.

Note: See CASAC paper, *Anomalies in the takeover provisions of the Corporations Law* (March 1994) at pp. 30–32 and the Explanatory Memorandum, Corporations Bill 1988, cl 1966.

RG 71.18 International comity considerations underpin the extension of the exemption in item 14 to downstream acquisitions occurring as a result of an acquisition in a foreign entity listed on an approved foreign exchange. This is because Australian securities regulation should not impose excessive costs or regulatory obstacles on primarily foreign corporate transactions.

## Scope of the exemption

RG 71.19 When considering whether a downstream acquisition is exempt from the prohibition in s606, persons acquiring a relevant interest in an upstream entity should be aware that:

- (a) the upstream entity must have a primary listing (and not only a secondary listing) on a prescribed financial market (including ASX) or an approved foreign exchange;
- (b) we will not consider that a downstream acquisition should be exempt from s606 merely because another exemption in s611 may apply to the upstream acquisition; and
- (c) a downstream acquisition may risk an application to the Takeovers Panel for a declaration of unacceptable circumstances even if it satisfies the exemption in item 14.

## Secondary listings

- RG 71.20 Class Order [CO 01/1542] *Relevant interests, voting power and exceptions to the main takeover prohibition* modifies item 14 to exclude secondary listings from the scope of the exemption. This is because the place of incorporation and the listing rules of the exchange on which the upstream entity has its primary listing may not satisfy the policy behind the exemption in item 14. This means that the item 14 exemption will not apply if the upstream entity only has a secondary listing on a prescribed financial market or on an approved foreign exchange: see [CO 01/1542].
- RG 71.21 Where a person makes an upstream acquisition and the upstream entity has only a secondary listing on a prescribed financial market or an approved foreign exchange, the acquirer may apply to us for individual downstream acquisition relief: see Section C.
- RG 71.22 We have approved a list of foreign exchanges for the purposes of item 14: see [CO 02/259]. For a discussion of when we may approve a new foreign exchange for the purposes of item 14, see RG 71.97–RG 71.99.

Note: A body with a secondary listing on ASX is referred to in the ASX Listing Rules as an ‘exempt foreign entity’.

## Upstream acquisitions where another exemption in s611 applies

- RG 71.23 We may not consider that a downstream acquisition should be exempt from s606 merely because another exemption in s611 applies to the upstream acquisition.
- RG 71.24 Downstream acquisitions will most often arise when a person makes a takeover offer for an upstream entity. There is an exemption from s606 for acquisitions that result from the acceptance of a takeover offer made under Ch 6: see item 1 of s611.
- RG 71.25 We do not consider that a downstream acquisition will be exempt from the prohibition in s606 merely because an exemption in s611 other than item 14 applies to the upstream acquisition. This is because there is a separate express exemption for downstream acquisitions in item 14. However, we acknowledge that there are different views on this issue.
- RG 71.26 An acquirer who cannot rely on item 14 but seeks to rely on another exemption in s611 in relation to a downstream acquisition may risk regulatory action by us, including an application to the Takeovers Panel for a declaration of unacceptable circumstances.

## Unacceptable circumstances

RG 71.27 A downstream acquisition may give rise to unacceptable circumstances even if it satisfies the exemption in item 14. An application to the Takeovers Panel for a declaration of unacceptable circumstances and orders (which include remedial orders) in relation to the affairs of a company can be made by ASIC or any other interested person: see Pt 6.10, Div 2, Subdiv B.

RG 71.28 Whether the circumstances of a downstream acquisition are unacceptable will depend on the particulars of each case. However, the Takeovers Panel will have regard to the purposes of Ch 6 set out in s602 when considering an application for a declaration of unacceptable circumstances. The Takeovers Panel stated in *Australian Pipeline Trust 01R* [2006] ATP 29 at [106] that:

... there is clear indication in the explanatory memoranda and the relevant extrinsic material (for the Corporations Act and its preceding legislation) that the legislature was concerned that the exemption set out in Item 14 not be abused and the intent of Chapter 6 not be avoided.

RG 71.29 The types of circumstances in which we may consider applying to the Takeovers Panel for a declaration of unacceptable circumstances despite the exemption in item 14 applying include where:

- (a) control of the downstream company is a significant purpose of the upstream acquisition (see, for example, the discussion in *Leighton Holdings Limited 02 R* [2010] ATP 14 at 67 and 70–86, and *Leighton Holdings 01, 02, 03* [2010] ATP 13 at 55); and/or

Note: If the downstream shares comprise over 50% of the assets of the upstream entity, the Takeovers Panel will consider if (among other factors) reliance on item 14 is unacceptable in the circumstances: see the discussion in *Leighton Holdings Limited 02 R* [2010] ATP 14.

- (b) the downstream acquisition technically satisfies the exemption in item 14 but subverts or otherwise does not meet the policy basis for reliance on the exemption in item 14, such as where the upstream entity is listed in name only and is closely held (see *Cape Lambert Minsec Pty Ltd* [2009] ATP 12 at 40).

## C When ASIC may grant relief

### Key points

Relief will be required where a downstream acquisition does not satisfy the exemption in item 14.

This section explains:

- our approach to relief (see RG 71.30–RG 71.33);
- when we may grant relief (see RG 71.35–RG 71.37);
- key concepts relevant to our decision whether to grant relief (see RG 71.38–RG 71.48); and
- when we will not grant relief (see RG 71.49).

### Our approach to relief applications

- RG 71.30 A person may apply for relief to make a downstream acquisition that would otherwise result in the person breaching s606. This will be required if the upstream entity is unlisted or does not have a primary listing on a prescribed financial market (such as ASX) or on an approved foreign exchange.
- RG 71.31 In deciding whether to grant relief for a downstream acquisition that does not satisfy the exemption in item 14, we will consider:
- (a) the policy objectives of the exemption in item 14 (see RG 71.16–RG 71.18); and
  - (b) the purposes of Ch 6, as set out in s602 (see RG 71.5–RG 71.6).
- RG 71.32 A prerequisite to relief will be compliance by the party applying for relief with the disclosure obligations discussed below.

### Disclosure obligations

- RG 71.33 Before we grant relief for a downstream acquisition that does not satisfy item 14, the applicant must satisfy us that the market for the shares in the downstream company is adequately informed about the upstream acquisition.
- RG 71.34 We will not grant relief unless the acquirer of the upstream entity discloses to the downstream company details about the timing and terms of the upstream acquisition at the time the upstream acquisition is announced. If the downstream company is listed, this will enable the downstream company to make an announcement to the relevant financial market about the upstream acquisition and the implications for the downstream shareholders. If the downstream company is not listed, the provision of this information will enable the downstream company to communicate directly with its members about the upstream acquisition and the potential implications of the upstream acquisition on the downstream company.

## When we may grant relief

RG 71.35 We may grant relief subject to conditions appropriate to the circumstances if we are satisfied that the policy and investor protections identified in this guide will be upheld.

RG 71.36 We will consider the following factors when deciding whether to grant relief:

- (a) whether the upstream entity is listed or unlisted. We will be more likely to grant relief if the upstream entity is listed;
- (b) international comity considerations;
- (c) whether control of the downstream company appears to be a significant purpose of the upstream acquisition or whether the downstream shares are a substantial part of the upstream entity's assets;

Note: If we grant relief despite these factors being present, we would be likely to impose a downstream bid condition to ensure that the principles in s602 will be upheld.

- (d) the alternatives that are available to the acquirer. There may be other ways to structure a transaction so that relief is not required, such as where the downstream shares can be simply and efficiently separated from the other assets of the upstream entity. In these circumstances, we may refuse relief as unnecessary. However, we understand that negotiations to separate the downstream shares from the assets of an upstream entity may be impracticable in the circumstances;
- (e) whether the regulation that applies to the upstream acquisition achieves similar regulatory outcomes to Australian takeovers regulation;
- (f) whether the upstream entity is widely or closely held:
  - (i) we will be unlikely to grant relief where the upstream entity is unlisted and closely held or listed in name only and closely held; and
  - (ii) where the upstream entity is closely held, it may also be easier for the acquirer to negotiate to separate the shares in the downstream company from the other assets of the upstream entity and relief would be unnecessary; and
- (g) any other circumstances that we consider relevant to the particular case.

RG 71.37 We may grant relief without conditions in rare and exceptional circumstances. The circumstances where we may grant relief without conditions are where:

- (a) we are in the process of approving the relevant financial market or foreign exchange for the purposes of item 14; or
- (b) the upstream entity has a secondary listing on a prescribed financial market or approved foreign exchange, which in the circumstances is effectively the primary regulation that applies to the upstream entity.

## Key concepts relevant to our decision about relief and conditions

- RG 71.38 When deciding whether to grant relief and the conditions that may apply, the following concepts are relevant:
- (a) whether control of the downstream company may be regarded as a significant purpose of the upstream acquisition (this is relevant to both whether we will grant relief and the conditions that may apply);
  - (b) whether the downstream shares are a substantial part of the upstream entity's assets (this is relevant to both whether we will grant relief and the conditions that may apply); and
  - (c) whether the acquirer will obtain effective control of the downstream company as a result of the upstream acquisition (this is relevant to the conditions that may apply).
- RG 71.39 For a discussion of the conditions that may apply to our relief, see Section D. For guidance on the information that should be provided to us when applying for relief, see Section E.

### Control purpose

- RG 71.40 If there is a control purpose in relation to the downstream company, we may refuse to grant relief, or grant relief subject to conditions that ensure that the principles in s602 will be upheld (such as requiring that the acquirer make a downstream bid).
- RG 71.41 When assessing whether control of the downstream company may be regarded as a significant purpose of the upstream acquisition, we will take into account all the relevant circumstances. These will include whether the circumstances suggest that the upstream acquisition has been structured or designed to avoid complying with Ch 6 in relation to the downstream company.
- RG 71.42 The following factors may suggest to us that control of the downstream company is a significant purpose of the upstream acquisition:
- (a) the percentage of shares in the downstream company held by the upstream entity, including whether the shares comprise a substantial part of the assets of the upstream entity;
  - (b) the voting power of the acquirer in the downstream company at the time of the application, as well as the voting power of the acquirer following the upstream acquisition;
  - (c) the nature of the assets of the upstream entity, other than the shares in the downstream company (i.e. whether they are highly liquid, or are readily procurable or saleable commodities otherwise than through the upstream acquisition);

- (d) any association or aggregation of relevant interests or voting power caused by the downstream acquisition; and
- (e) cross-shareholdings, common board memberships and any other common significant management or other relevant relationships between any of the following:
  - (i) the acquirer;
  - (ii) the upstream entity;
  - (iii) the downstream company; or
  - (iv) their associates.

### **Substantial assets**

- RG 71.43 If the downstream shares comprise a substantial part of the assets of the upstream entity, we may refuse relief or grant relief subject to conditions that ensure that the principles in s602 will be upheld (such as requiring that the acquirer make a downstream bid).
- RG 71.44 We will normally regard 50% of the upstream entity's assets as the threshold for determining whether the downstream shares constitute 'a substantial part of the assets of the upstream entity'. If the market value of the downstream shares constitutes more than 50% of the value of the assets of the upstream entity, we will be more likely to determine that control of the downstream company is a significant purpose of the upstream acquisition.
- RG 71.45 While 50% or more of the assets of the upstream entity is the threshold for determining whether the downstream shares constitute a substantial part of the assets of the upstream entity, we may choose to lower this figure taking into account the practical circumstances of the proposed acquisitions (e.g. if the upstream entity has significant cash assets).

### **Effective control**

- RG 71.46 If the acquirer will obtain effective control of the downstream company as a result of an upstream acquisition, any relief granted would generally be subject to a condition that the acquirer make a downstream bid for the downstream company.
- RG 71.47 When determining whether the acquirer will obtain effective control of the downstream company, we will generally regard voting power of 50% or above as constituting effective control. This is because the acquirer will have absolute or effective control over the downstream company with control over 50% or more of the voting shares.
- RG 71.48 We may choose a figure lower than 50% if it appears to us that effective control over the downstream company, such as is envisaged under s50AA or

the accounting standards dealing with controlling entities, may be exercised with less than 50% of the voting shares in the downstream company. We will also consider the circumstances of the downstream company, including the share register and whether there are any other substantial shareholdings in the downstream company.

## When we will not grant relief

- RG 71.49 We will not grant relief to facilitate a downstream acquisition where:
- (a) relief would be inconsistent with the policy behind the exemption in item 14 and the principles in s602; or
  - (b) after considering all the relevant circumstances, we are not satisfied that the regulatory detriment is minimal or clearly outweighed by the resulting commercial benefit (see Regulatory Guide 51 *Applications for relief* (RG 51), in particular RG 51.57–RG 51.62); or
  - (c) the upstream acquisition is not legal in the jurisdiction where it is to take place; or
  - (d) it appears to us that the downstream acquisition may give rise to unacceptable circumstances.

## D Conditions of relief

### Key points

This section explains the factors we will consider when determining the types of conditions that may apply to our relief: see RG 71.50–RG 71.53.

The conditions that may apply to our relief are:

- a downstream bid condition (see RG 71.54–RG 71.73); or
- standstill and voting conditions (see RG 71.74–RG 71.82); and/or
- other conditions instead of, or in addition to, these conditions, including a sell-down condition (see RG 71.83–RG 71.86).

### What conditions may apply?

RG 71.50 Before we grant relief to allow a downstream acquisition that does not satisfy item 14, the applicant must satisfy us that the market for the shares in the downstream company will be adequately informed about the upstream acquisition. This will generally require the applicant to comply with certain disclosure obligations: see RG 71.33–RG 71.34.

RG 71.51 Where we grant relief to allow a downstream acquisition that does not satisfy the exemption in item 14, our relief will be subject to:

- (a) a downstream bid condition; or
- (b) standstill and voting conditions; and/or
- (c) other types of conditions (including a sell-down condition) instead of, or in addition to, the above conditions on a case-by-case basis.

RG 71.52 When determining the conditions that should apply, we will consider:

- (a) whether control of the downstream company may be regarded as a significant purpose of the upstream acquisition (see RG 71.40–RG 71.42);
- (b) whether the downstream shares represent a substantial part of the assets of the upstream entity (see RG 71.43–RG 71.45);
- (c) whether the downstream shares to be acquired through the upstream acquisition will give the acquirer effective control of the downstream company (see RG 71.46–RG 71.48);
- (d) the effect of the acquisition on the other downstream shareholders;
- (e) whether the conditions are practical in the circumstances; and
- (f) any other circumstances that we consider relevant to the particular case.

Note: When calculating the downstream shares to which the upstream acquirer is entitled to, or becomes entitled to following the downstream acquisition, we will include the shares and interests in the downstream company referred to in RG 71.42.

RG 71.53 Table 1 summarises the different types of conditions that may apply to our relief.

**Table 1: Conditions that may apply**

Conditions	When they may apply
<p><b>Downstream bid condition</b> (see RG 71.54–RG 71.73)</p>	<p>This condition will generally apply when:</p> <ul style="list-style-type: none"> <li>• control of the downstream company appears to be a significant purpose; or</li> <li>• downstream shares are a substantial part of the upstream entity's assets; or</li> <li>• effective control of the downstream company will be obtained.</li> </ul>
<p><b>Standstill and voting conditions</b> (see RG 71.74–RG 71.82)</p>	<p>These types of conditions will generally apply when:</p> <ul style="list-style-type: none"> <li>• control of the downstream company does not appear to be a significant purpose;</li> <li>• downstream shares are not a substantial part of the upstream entity's assets; and</li> <li>• effective control of the downstream company will not be obtained.</li> </ul>
<p><b>Other types of conditions (including a sell-down condition)</b> (see RG 71.83–RG 71.86)</p>	<p>We will apply other types of conditions on a case-by-case basis, as appropriate. These conditions may be instead of, or in addition, to the above conditions.</p>

## Downstream bid condition

RG 71.54 A downstream bid condition will require the acquirer to make a takeover bid for the downstream company on terms consistent with the policy set out below. The purpose of the downstream bid condition is to ensure that, as far as is practicable, the downstream shareholders share equally in the benefits being offered to the upstream holders under the upstream acquisition. Our guidance on the terms of the downstream bid is based on the Federal Court decision in *BTR Plc v Westinghouse Brake and Signal Co (Australia) Ltd* (1992) 106 ALR 35.

RG 71.55 Where our relief is subject to a downstream bid condition, we may also impose a voting condition that would generally prevent the acquirer from being able to exercise, or procure the exercise of, the votes attached to the downstream shares in excess of 20% until the close of the downstream bid. This condition is to ensure fairness between the acquirer and the other downstream shareholders during the downstream bid period.

## **Type of bid**

- RG 71.56 A downstream bid must be an offer to acquire all (and not a specified proportion) of the bid class securities that the acquirer does not otherwise have a relevant interest in and that exist or will exist at the date specified in the bidder's statement lodged with ASIC.

## **Pricing of downstream bid**

- RG 71.57 We will normally require a downstream bid to be cash or include a cash alternative that is not less than the fair value ascribed to the downstream shares by an independent expert approved by us, or the 'effective' price.

## **'Effective' price**

- RG 71.58 If the price effectively being offered to the upstream shareholders for the shares in the downstream company held by the upstream entity can be clearly and accurately determined from the upstream acquisition price, we will allow the downstream bid to be made at the 'effective' price (i.e. where the upstream entity is a listed investment entity and the upstream acquisition price does not indicate that the market price for each of the investments is unreliable).
- RG 71.59 We reserve the discretion in such cases to alter the pricing mechanism for the downstream bid if later information indicates that the 'effective' price paid for the downstream shares is not as transparent as represented to us in the application. Any uncertainty about the price will be reduced if we have the opportunity to obtain submissions from third parties who may be affected by our decision before we alter the pricing mechanism for the downstream bid. These submissions would be on the mechanism for determining the price of the downstream bid.
- RG 71.60 If the upstream acquisition price is 'see-through' and is increased during the course of the upstream acquisition, the increase must be reflected in an increase in the downstream bid price.

## **Independent expert's valuation to determine fair value**

- RG 71.61 It will often not be possible to clearly and accurately determine the 'effective' price being offered for the downstream shares from the upstream acquisition price. Where this is the case, we will generally require that the consideration for the downstream bid must not be less than the fair value ascribed to the shares in the downstream company as determined by an independent expert approved by us.

- RG 71.62 In determining the fair value of shares in the downstream company:
- (a) the independent expert should follow the guidance in Regulatory Guide 111 *Content of expert reports* (RG 111);
  - (b) the independent expert must determine the value per share, inclusive of a premium for control, regardless of percentage ownership of the downstream company (as this valuation method, by definition, distributes any control premium equally between all shareholders);
  - (c) the independent expert must determine the value per share on the basis of information that was available to the acquirer at the time the acquirer was fixing the price of the upstream acquisition (the independent expert is not limited to information that was used by the acquirer);
  - (d) the acquirer must ensure that the independent expert is provided with all information about the downstream company that was available to the acquirer when the acquirer was fixing the price of the upstream acquisition;
  - (e) the independent expert report must include a prominent statement that:
    - (i) the purpose of the report is to set the price of the downstream bid and has not been prepared for the purpose of providing an opinion as to whether the downstream bid is fair and reasonable within the meaning of s640; and
    - (ii) that the report has been prepared on the basis of information available to the acquirer at the time the upstream acquisition price was fixed and therefore will not take into account any new circumstances that occur in relation to the downstream company, which may affect the fair value of the downstream shares;
  - (f) the acquirer of the upstream entity must pay the independent expert's fees; and
  - (g) the independent expert's report must be included in the acquirer's bidder's statement for the downstream company.
- RG 71.63 If the independent expert gives a range of values, calculated by one valuation methodology, generally the price shall be the midpoint of the range. This is because, where it is not possible to determine an 'effective' price, the independent expert report serves the function of determining a fair value for the downstream shares. If the independent expert gives different values or different midpoints calculated by different methodologies, we consider that the highest value or highest midpoint should be used. We may consider requests to vary the terms of the relief for the selection of the downstream bid price and will consider the independent expert's advice in determining these applications.
- RG 71.64 The independent expert must determine the fair value of the downstream shares as at the time when the acquirer was fixing the price of the upstream acquisition. If the price of the upstream acquisition is subsequently increased, the expert must determine the fair value of the downstream shares at the time

of the increase and prepare a revised independent expert report. If necessary, the price of the downstream bid must be increased so that it is at least equal to this new value.

RG 71.65 In this situation, we will generally require the preparation of a revised independent expert report (which may be done by way of a supplementary report), and the value of the downstream bid must not be less than the updated fair value of the downstream shares as at the time when the acquirer was fixing the increased price of the upstream acquisition.

RG 71.66 New circumstances may arise during the downstream bid period that could have a material impact on the independent expert's assessment of the fair value of the downstream company's shares. Where the price of the upstream acquisition is not increased as a result of the new circumstances, we will not require the downstream bid price to be increased because there is no increase in the benefit being offered to the upstream shareholders. We consider that it may be appropriate for the independent expert to make a statement as to the status of the independent expert report in light of the new circumstances.

RG 71.67 The new circumstances may be information that downstream shareholders and their professional advisers might reasonably require to make an informed assessment whether to accept the downstream bid. Accordingly, the directors of the downstream company will need to:

- (a) consider whether to revise their recommendation in relation to the downstream bid; and
- (b) provide shareholders with a supplementary target's statement explaining the effect of the new circumstances and consider whether valuation information should be provided where the new circumstances affect whether the downstream bid price is fair or reasonable.

### **Other terms of downstream bid**

RG 71.68 We will normally require a downstream bid to meet the following other conditions:

(a) *Duration*

The legislature has determined that one month is the minimum period to satisfy s602(b): see s624(1)(b). However, if an acquirer makes its downstream bid before the upstream acquisition becomes unconditional, the acquirer must ensure that its downstream bid remains open long enough for shareholders to consider that bid in light of significant events in the upstream acquisition. The downstream bid should remain open for at least two weeks after the acquirer becomes unconditionally entitled to more than 20% of the voting shares in the upstream entity or the upstream acquisition becomes unconditional (whichever is the later).

(b) *Dispatch*

Offers must be dispatched no later than four weeks after the acquirer becomes entitled to more than 20% of the voting shares in the upstream entity or the upstream acquisition is declared unconditional (whichever is the earlier).

Note: If an upstream offer is made in a foreign jurisdiction where the takeover threshold is greater than 20%, we may increase the relevant references in this guide to 20% of the voting shares in the upstream entity.

**Permissible defeating conditions of downstream bid**

RG 71.69 Our relief will normally limit the defeating conditions that the acquirer may place on the downstream bid. However, provided that it undertakes in its offer to use its best endeavours to satisfy them, our relief will generally allow an acquirer to impose the following defeating conditions on its downstream bid:

- (a) the upstream acquisition is successful (providing that success is defined as being unconditionally entitled to more than 20% of the voting shares in the upstream entity);
- (b) no prescribed occurrence occurs. The condition may relate to events that occur from the date of the announcement of the upstream acquisition, but must be worded to lapse once the acquirer has achieved control of the downstream company via the upstream acquisition; and
- (c) requisite regulatory approval is gained (e.g. from the Foreign Investment Review Board or the Australian Competition and Consumer Commission (ACCC)).

RG 71.70 We will not allow a downstream bid to be subject to a defeating condition for minimum acceptances or that the acquirer achieve the thresholds for compulsory acquisition set out in s661A(1).

Note: In *BTR Plc v Westinghouse Brake and Signal Co (Australia) Ltd* (1992) 106 ALR 35 (BTR case), the Federal Court held that the predecessor of ASIC, the Australian Securities Commission (ASC), was entitled to refuse to permit an acquirer to make a downstream bid subject to a compulsory acquisition condition.

**Related relief for downstream company—Expert report under s640**

RG 71.71 To satisfy s640, the downstream target may be required to provide an expert report that states whether in the expert's opinion, the takeover offers are fair and reasonable and gives the reasons for forming that opinion. We may exempt the downstream target from the provisions of s640 if the expert report is required only because the acquirer became a major shareholder of the downstream company as a result of the upstream acquisition. In these cases, the protection of an expert report under s640 is not required. Also, the

pricing of the downstream bid would have been determined in accordance with our policy.

- RG 71.72 This relief may be inappropriate if material changes to the target company occur between the date of the expert's report and the date for dispatch of the target's statement.
- RG 71.73 We will not grant this relief where s640 would require an expert report for any reason other than that the acquirer became a major shareholder of the downstream company as a result of the upstream acquisition. In these cases, the acquirer may be assumed to have had access to confidential information about the downstream company and to have been in a position to control or influence the actions and responses of both the target boards for the duration of the offer.

## Standstill and voting conditions

- RG 71.74 Where our relief is subject to standstill and voting conditions, we will consider whether the acquirer will obtain absolute or effective control of the 'upstream entity' before deciding what types of standstill and voting conditions will apply.
- RG 71.75 Where the acquirer will obtain absolute or effective control of the upstream entity (e.g. the acquirer will acquire a relevant interest in 80% of the upstream entity, which holds a relevant interest in 20% of the shares in the downstream company), our relief will be subject to:
- (a) a 'standstill condition' that, for a specified period (see RG 71.77), the acquirer will not acquire, or procure the upstream entity to acquire, a relevant interest in any more shares in the downstream company; and
  - (b) a 'voting condition' that, for the specified period, the acquirer will not exercise, control the exercise, or procure the exercise, of any votes attached to the shares in the downstream company in which it acquired a relevant interest in as a result of the upstream acquisition.
- RG 71.76 Where the acquirer will not obtain absolute or effective control of the upstream entity (e.g. the acquirer will acquire a relevant interest in 30% of the upstream entity, which holds a relevant interest in 20% of the shares in the downstream company), our relief will be subject to:
- (a) a standstill condition that, for a specified period (see RG 71.77), the acquirer will not acquire a relevant interest in any more shares in the downstream company, other than an increase in the relevant interest arising because the upstream entity increases its relevant interest in the downstream company under an exemption in s611, such as item 7 or item 9; and

- (b) either:
- (i) a voting condition that applies to the upstream entity for the specified period, where the upstream entity supports the application and agrees to such a condition being imposed; or
  - (ii) some other type of condition, such as a condition that the acquirer must not procure the exercise of any votes attached to the downstream shares it acquired a relevant interest in as a result of the upstream acquisition during the specified period.

- RG 71.77 The specified period will be equivalent to the minimum period of time within which the applicant could have acquired the same number of voting shares using the 3% creep exemption in item 9 of s611.
- RG 71.78 The purpose of standstill and voting conditions is to protect the interests of downstream company shareholders in circumstances where the upstream acquirer has obtained a relevant interest in more than 20% of the downstream company. The interests of downstream shareholders are protected because standstill and voting conditions reduce the control effect of the downstream acquisition.
- RG 71.79 We consider that different types of standstill and voting conditions should apply depending on whether the acquirer obtains absolute or effective control of the upstream entity. This is because, where the acquirer obtains absolute or effective control of the upstream entity, the acquirer is in a position to control the affairs of the upstream entity, including decisions about acquiring a further relevant interest in the shares of the downstream company and exercising, controlling, or procuring the exercise by the upstream entity of, the votes attached to the shares in the downstream company.
- RG 71.80 In contrast, we consider that less restrictive standstill and voting conditions are appropriate where the acquirer does not obtain absolute or effective control of the upstream entity. In these cases, we consider that a less restrictive standstill condition is appropriate because of the impact such a condition may have on the upstream company (i.e. in these cases, our relief should not prevent the upstream entity from relying on exemptions in s611 that would otherwise be available). In addition, we consider that a voting condition may be of limited benefit because it will be the upstream entity not the acquirer that will control the power to exercise the votes attached to the downstream shares.
- RG 71.81 In relation to applying a voting condition on the upstream entity, we acknowledge that this may cause the potential for conflicts of interest to arise for the directors of the upstream entity. However, we consider that this condition or an appropriate alternative condition (such as the one discussed at RG 71.76(b)(ii)) will ensure that the interests of downstream shareholders are adequately protected.

RG 71.82 When considering whether to impose standstill and voting conditions on our relief, we will consider all the relevant circumstances, including submissions from the upstream entity. We will also consider the impact of the conditions on the downstream company, including their impact on the distribution of voting power in the downstream company. We will take into account the aim of protecting the interests of downstream holders by reducing the effect of the upstream acquisition on control of the downstream company and the effect of our relief on the upstream entity. When granting relief, we aim to reduce the risk that our relief is abused by seeking to ensure that an acquirer is not permitted to act in a manner contrary to the basis on which our relief was granted.

## Other conditions that may apply

RG 71.83 We may consider that the conditions discussed above are not appropriate in the circumstances of a particular application. We may also consider that, given the particular circumstances of a proposed downstream acquisition, other conditions should apply to our relief in addition to standstill, voting or downstream bid conditions. We may apply other conditions to our relief on a case-by-case basis.

### Sell-down condition

RG 71.84 One type of condition we may consider applying as an alternative to a downstream bid condition is a sell-down condition. We expect that we will grant relief subject to a sell-down condition in limited circumstances.

Note: When considering whether to impose a sell-down condition, we may consult with affected third parties such as the downstream company and substantial shareholders of the downstream company.

RG 71.85 Where our relief is subject to a sell-down condition, the condition will require the acquirer to sell down its interest in the downstream company within a specified time (and if this is not achieved, the acquirer or a subsidiary will be required to make a downstream bid consistent with the policy in this guide).

RG 71.86 If the acquirer is required to sell down its interest in the downstream company, our condition will normally state that the acquirer must:

- (a) appoint a broker to reduce the acquirer's voting power in the downstream company to 20% or less within 14 days of acquiring control of the upstream entity (or otherwise acquiring the power to control the disposal of the downstream shares);
- (b) not exercise, or procure the exercise of, any voting rights attached to the downstream shares in excess of 20% without our consent; and

- (c) in selling any downstream shares acquired under the relief, ensure that the broker appointed uses its best endeavours to obtain as wide a placement as practicable, for the highest practicable price.

## E Applying for relief

### Key points

This section sets out the process for applying for relief from s606 in relation to a downstream acquisition that does not satisfy the exemption in item 14.

### How to apply for relief

- RG 71.87 We have discretionary power to grant relief from the requirements of Ch 6 in the form of an exemption from specified provisions, or a declaration that varies or modifies specified provisions as they apply to a person: see s655A.
- RG 71.88 Downstream acquisitions generally involve complex transactions and issues. Applicants should ensure that there will be sufficient time for us to consider an application for individual downstream acquisition relief. Applications should normally be lodged no later than 28 days before the relevant upstream acquisition is to be made. Additional time should be allowed for applications that are outside the scope of our existing policy.
- RG 71.89 Applicants seeking relief should approach us before the upstream acquisition takes place. We do not generally have power to grant retrospective relief. This means that we are unlikely to grant relief to allow a downstream acquisition if a breach of s606 has already occurred. Applicants should also refer to RG 51 before deciding on a course of action or timetable for any acquisition.
- RG 71.90 Applications may be lodged, with the relevant fee, at any ASIC office and/or by email to [applications@asic.gov.au](mailto:applications@asic.gov.au).

### Information applicants should provide

- RG 71.91 When applying for relief, applicants should refer to Section C and Section D of this guide and provide full particulars of the proposed upstream and downstream acquisitions (including the timing, extent and price of the proposed acquisitions) and drafts of the relevant upstream acquisition transaction documents.
- RG 71.92 An applicant should also provide particulars of:
- (a) its voting power in the downstream company at the date of its application; and
  - (b) all acquisitions and disposals, by the applicant and any associate, of securities in the downstream company and in the upstream entity in the four months before the date of its application.

- RG 71.93 To assist us in determining whether control over the downstream shares is a significant purpose of the upstream acquisition, applicants must provide us with:
- (a) a clear breakdown of the assets of the upstream target with absolute and percentage values for the major items and for the downstream shares;
  - (b) information as to the intrinsic value of the assets of the upstream target to the acquirer other than the downstream shares; and
  - (c) a list of the top 20 shareholders of the downstream company, and any associations between them and the applicant.
- RG 71.94 An application should clearly explain the regulatory regime under which the upstream acquisition will take place. The application should especially explain:
- (a) the disclosure regime; and
  - (b) the nature of any provisions equivalent to the principles in s602 and provisions equivalent to s621 and 623.

## Procedural fairness

- RG 71.95 In some circumstances, we will consider that we are required to consult with the downstream company, the shareholders of the downstream company or other potentially adversely affected third parties: see Regulatory Guide 92 *Procedural fairness to third parties* (RG 92).
- RG 71.96 The directors of the target company will normally be assumed to be suitable representatives of the interests of the downstream shareholders. However, this may not be the case where:
- (a) the acquirer of the upstream entity has been a substantial shareholder of the upstream target and the upstream target has been in a position to control or influence the composition of the board of the downstream company;
  - (b) the acquirer has been in a position to control the downstream board in any other way; or
  - (c) there is evidence or we have been made aware of a dispute between shareholders and the board of the company about the management and corporate governance of the company.

## Approving a foreign exchange

- RG 71.97 We have approved a list of foreign exchanges for the purposes of item 14: see [CO 02/259]. Unless otherwise stated, our relief applies to the main board of these markets (e.g. our relief will not extend to debt listings).
- RG 71.98 In approving the list of foreign exchanges included in [CO 02/259] we took into account the criteria set out at RG 72.54, because the extension of the item 14 exemption to foreign exchanges that meet these criteria satisfies the policy behind the exemption in item 14: see RG 71.17.
- RG 71.99 A foreign body conducting an exchange may apply to us for approval for the purposes of item 14. A foreign body corporate may also apply, but the assistance of the foreign body conducting the exchange is highly desirable. An application to approve a new foreign exchange will be a new policy application: see RG 51 for guidance on making new policy applications.

## Key terms

Term	Meaning in this document
ASIC	Australian Securities and Investments Commission
ASX	ASX Limited (ACN 008 624 691) or the exchange market operated by ASX Limited
ASX Listing Rules	The listing rules of ASX
CASAC	The Legal Committee of the Companies and Securities Advisory Committee
Ch 6	A chapter of the Corporations Act (in this example, numbered 6)
[CO 02/259] (for example)	An ASIC class order (in this example, numbered 02/259)
Corporations Act	<i>Corporations Act 2001</i> , including regulations made for the purposes of that Act
downstream acquisition	Acquisition of a relevant interest in the shares of a downstream company as a result of an acquisition in an upstream entity
downstream company	An Australian company, listed body or listed managed investment scheme with some of its shares or voting interests owned by an upstream company
effective price	A price for the downstream shares that is able to be clearly and accurately determined from the upstream acquisition price
item 14	Item 14 of s611 of the Corporations Act
Pt 5.1	A part of the Corporations Act (in this example numbered 5.1)
relevant interest	Has the meaning given by s608 and 609 of the Corporations Act
RG 51 (for example)	An ASIC regulatory guide (in this example, numbered 51)
s611 (for example)	A section of the Corporations Act (in this example, numbered 611), unless otherwise specified
sell down	An acquirer reduces its voting power in a downstream company
standstill condition	A condition that we may impose on our relief preventing the acquirer from acquiring a relevant interest in any more shares in the downstream company

Term	Meaning in this document
Takeovers Panel	The panel established under s171 of the <i>Australian Securities and Investments Commission Act 2001</i> and given various powers under Pt 6.10 of the Corporations Act
upstream acquisition	Acquisition of a relevant interest or control in an Australian or foreign upstream entity
upstream entity	An Australian or foreign company or body corporate or managed investment scheme that holds shares in a downstream company or voting interests in a downstream Australian listed managed investment scheme
voting condition	A condition that we may impose on our relief preventing the acquirer (and in some circumstances, the upstream entity) from exercising or procuring the exercise of any votes attached to the shares in the downstream company
voting power	Has the meaning given in s610 of the Corporations Act
voting share	Has the meaning given in s9 of the Corporations Act

## Related information

### Headnotes

conditions of relief, disclosure to market, downstream acquisition, downstream company, foreign body, international comity, listed companies, policy for granting relief, prohibition on breach of ‘20% threshold’, takeovers, unacceptable circumstances, unlisted companies, upstream acquisition, upstream entity

### Class orders

[CO 01/1542] *Relevant interests, voting power and exceptions to the main takeover prohibition*

[CO 02/259] *Downstream acquisitions: foreign stock markets*

[CO 05/84] *JSE Securities Exchange South Africa added to ASIC’s downstream acquisition takeover relief*

### Regulatory guides

RG 51 *Applications for relief*

RG 72 *Foreign securities prospectus relief*

RG 92 *Procedural fairness to third parties*

RG 111 *Content of expert reports*

### Legislation

Corporations Act, s50AA, 602(b), 602(c), 606, 608, 608(3)(a), 608(3)(b), 608(4), 608(5), 611 (items 1 and 14), 621, 623, 624(1)(b), 640, 655A, 655A(1), 655A(2), 657A, 661A(1)

### Cases

*Australian Pipeline Trust 01* [2006] ATP 29

*BTR Plc v Westinghouse Brake and Signal Co (Australia) Ltd* (1992) 106 ALR

*Cape Lambert Minsec Pty Ltd* [2009] ATP 12

*Leighton Holdings Limited 01, 02 and 03* [2010] ATP 13

*Leighton Holdings Limited 02 R* [2010] ATP 14

## **Reports**

CASAC, March 1994, *Anomalies in the takeovers provisions of the Corporations Law*