ASIC

Australian Securities & Investments Commission

CONSULTATION PAPER 43

Finalising Interim Policy Statement 159 Takeovers: Discretionary powers

February 2003

Your comments

You are invited to comment on the proposals and issues for consideration in this paper. All submissions will be treated as public documents unless you specifically request that we treat the whole or part of your submission as confidential.

Comments are due by Friday 4 April 2003 and should be sent to:

Andrew Fawcett, Senior Lawyer
Regulatory Policy Branch
Australian Securities & Investments Commission
GPO Box 5179AA
Melbourne VIC 3000
facsimile: 03 9280 3306
email: andrew.fawcett@asic.gov.au

You can also contact the ASIC Infoline on 1300 300 630 for information and assistance.

What this policy proposal paper is about

1 We are turning Interim Policy Statement 159 *Takeovers: Discretionary powers* (IPS 159) into a final policy statement. This policy proposal paper sets out our proposals for finalising and updating IPS 159. Interim Policy Statement 159 was originally issued in March 2000, when the *Corporate Law Economic Reform Program Act 1999* (CLERP Act) commenced. We released IPS 159 as an interim policy because we intended to review it in light of our experience of the CLERP Act.

2 Interim Policy Statement 159 discusses how we will use our discretionary powers to exempt from or modify the takeover provisions introduced by the CLERP Act. It sets out:

(a) our policy on issues we expect may commonly be the subject of applications for relief from the takeover provisions after commencement of the CLERP Act; and

(b) the status of our pre-CLERP Act policies.

3 This policy proposal paper discusses:

(a) proposed amendments to certain interim policies in IPS 159; and

(b) proposed additional policies to address various issues raised with us since March 2000.

Amendments to interim policy

4 In our final policy, we are proposing to amend our interim policy in IPS 159 relating to:

(a) classes of securities (topic C of IPS 159 and **topic D** of this paper);

(b) changes to a bidder's statement between lodgment and dispatch (topic F of IPS 159 and **topic J** of this paper); and

(c) approval of notices of variation (topic N of IPS 159 and **topic K** of this paper).

5 In our final policy, we will also make technical amendments to the balance of IPS 159 to reflect changes introduced by the *Corporations Act 2001* (Act) and the *Financial Services Reform Act 2001*.

Additional policy

6 In our final policy, we are also proposing to add topics that are not currently discussed in IPS 159, including:

(a) escrows (**topic A** of this paper);

(b) non-transferable securities (**topic B** of this paper); and

(c) exercise of convertible securities acquired under a bid (**topic C** of this paper).

Status of proposals

7 The policy proposals in this paper are not final policy. After consultation on the proposals, we will update and publish our final policy as Policy Statement 159. Until this time, our interim policy as set out in IPS 159 continues to apply.

Contents

Policy proposals

In this paper, there are 11 groups of policy proposals for finalising IPS 159. For each group, we set out the proposals and identify issues we would like you to comment on. When necessary, we have also included some explanations of our proposals.

A Escrow

Policy proposal	Your feedback
ASX escrow	
A1 We propose to give class order relief modifying s609 so that a listed company does not have a relevant interest in securities merely because the company is required to apply restrictions on the disposal of securities under the ASX Listing Rules Chapter 9 ("ASX escrow"). This is for the purposes of the takeover provisions in Chapter 6 and substantial holding provisions in Chapter 6C.	
A2 For certainty, we will also give class order relief clarifying that ASX does not have a relevant interest merely because it has the power to consent to the release of securities from ASX escrow. ASX has this power in the case of a takeover bid or scheme of arrangement: Listing Rule 9.17.	
Voluntary escrow	
A3 We propose to give case-by-case relief modifying s609 so that a company does not have a relevant interest merely because it enters into an escrow with a holder that is not an ASX escrow. Our relief would apply where the holder is a person to whom the company issues securities in return for services or assets ("voluntary escrow"). Our relief will be from the takeover prohibition in s606, not the substantial holding provisions in s671B.	**A3Q1** Should we give relief where the escrow is not mandatory? **A3Q2** Should our relief extend to substantial holding provisions on the basis that ASX Listing Rule disclosure requirements concerning escrow extend to voluntary escrows?
A4 The voluntary escrow must: (a) restrict disposal and not voting; (b) terminate no later than 24 months after the securities are issued; and (c) allow the holder to accept into a takeover	**A4Q1** Is 24 months an appropriate limit? Or should a shorter period be chosen? **A4Q2** Should our relief require that escrow allows the holder to accept only in the case of a

Policy proposal	Your feedback
bid and allow the securities to be transferred or cancelled as part of a merger by scheme of arrangement.	successful bid: acceptance for at least 50% of shares not subject to escrow?
A5 If the securities are issued under a prospectus, we will require that details of the escrow are disclosed in the prospectus. If the issue of the securities is approved at a meeting of holders (eg under item 7 of s611), we will require that details are disclosed in the notice of meeting or explanatory statement accompanying the notice.	
Underwriter escrow	
A6 We propose to give case-by-case relief from the takeover provisions in Chapter 6, modifying s609, so an underwriter does not have a relevant interest in securities in a company merely because it has required that the company's controller or substantial holder enter into an escrow ("underwriter escrow"). An underwriter in a "sell-down" or "spin-off" transaction may require that the controller enter into an escrow preventing the controller from selling more securities in the period immediately after the public offering.	
A7 The underwriter must enter into the underwriting in the ordinary course of its business of underwriting. The underwriter escrow must: (a) restrict disposal and not voting; and (b) terminate no later than 6 months after the public offering. Details of the escrow must be disclosed in any prospectus or explanatory statement.	**A7Q1** Is 6 months a reasonable limit?

Explanation

Relevant interest

1 Without our relief, a person who enters into an escrow with a holder has a relevant interest in the securities subject to the escrow because the person controls exercise of the power to dispose of the securities: s608(1)(c). Subsection 609(7) underlines that a person has a relevant interest in securities if they may restrict the disposal of the securities. The subsection states that a person does not have a relevant interest in securities because of an agreement if the agreement does not restrict disposal of the securities for more than 3 months from the date when the agreement is entered into: s609(7)(c).

2 Subsection 608(9) states that s608 may result in a body corporate having a relevant interest in its own securities. This confirms that a company may have a relevant interest in its own securities that are subject to escrow.

ASX escrow

Rationale

3 Entering into an ASX escrow cannot effect a change of control over a company, as opposed to the acquisition by the holder of the securities the subject of the escrow.

4 Our proposed class order relief for ASX escrow requirements would facilitate the "fair, orderly and transparent market" benefits of these requirements: s792A.

5 The ASX escrow is designed to align:

(a) the interests of a vendor of an asset to the company, a seed capitalist, a promoter, a professional or a consultant rewarded by the company with securities; and

(b) the interests of other holders.

6 ASX states:

> "For example, escrow delays the time in which a vendor can realise the value of the securities. The delay allows the value of assets or services sold to an entity to become more apparent, and for the market price of the entity's securities to adjust before the vendor receives full consideration. In that way, the business risk is shared between the vendor and other investors": ASX Guidance Note 11 *Restricted Securities and Voluntary Escrow* paragraph 2.

7 The escrow may promote an orderly market in the securities by preventing a sell-down of a substantial number of securities immediately after the securities are issued.

ASX Listing Rules

8 ASX Listing Rules state that listed companies falling outside the scope of Listing Rule 9.1.3 must apply restrictions on disposal to holders of restricted securities and enter into a restriction agreement (escrow), so that the holder may not deal with the securities for a specified time of either 12 or 24 months: see Listing Rules 9.1 and 9.2. The company must also take steps to restrict transfer of the securities either by lodging certificates with a bank or applying a holding lock in CHESS: Listing Rules 9.5 and 9.14. "Restricted securities" are securities issued to a vendor of an asset to the company, a seed capitalist, a promoter, a professional or consultant subject to the restrictions in Chapter 9 of the Listing Rules.

9 ASX may consent to the release of the securities from escrow to enable the holder to accept a takeover bid or to enable the securities to be transferred or cancelled as part of a merger by way of scheme of arrangement: Listing Rule 9.17. Conditions include that in a takeover bid, holders of at least half of the bid class securities that are not restricted securities have accepted: Listing Rule 9.18.

ASX relief

10 For certainty our proposed class order would give relief to ASX because ASX restricts the holder from disposing of securities and has the power to consent to the release of securities from an ASX escrow in the case of a takeover bid or scheme of arrangement. ASX may have a relevant interest in the securities because it has the power to control disposal of the securities: s608(2)(c) and 608(7).

Voluntary escrow

Rationale

11 Entering into a voluntary escrow cannot effect a change of control. A company may require a voluntary escrow to align the interests of a person to whom it issues shares with the interests of other holders and to promote an orderly market for the shares. The period and terms of a voluntary escrow should be limited. The benefits of an escrow must be balanced against its potential defensive effect.

12 This is particularly where securities subject to escrow constitute a substantial interest in the company. Holders of these securities may be prevented from accepting into a takeover bid.

13 Even where holders are free under the terms of the voluntary escrow to accept into a takeover bid or to accept into a successful takeover bid, the escrow may have a defensive effect. A potential bidder may be discouraged because they are unable to build a pre-bid stake or to obtain over 50% of securities other than securities the subject of the escrow.

Examples of voluntary escrow

14 A company may wish to enter into a voluntary escrow with a person to whom it issues securities in return for services or assets provided to the company. The escrow may not be an ASX escrow for reasons including:

(a) the company is not listed;

(b) the ASX restricted securities requirements may not apply. For example, the requirements may not apply in the case of a listed company because it is admitted under the profit test in ASX Listing Rule 1.2, has a track record of profitability or revenue or has a substantial proportion of tangible assets: Listing Rule 9.1.3;

(c) a company that is already listed has placed securities to an investor for cash and wishes to prevent a sell-down by the investor; or

(d) a company that is already listed acquires another business and issues securities to a director or senior manager of that business. The director or manager is not a vendor, seed capitalist, promoter or professional to whom the ASX escrow requirements apply.

New securities only

15 Our proposed relief would apply only where the securities that go into voluntary escrow are newly issued. This is because the rationale of aligning the interests of vendors or promoters with other holders and allowing time for the value of assets and services to become apparent applies only to new securities: see paragraphs 4–6 of this topic.

Defensive purpose

16 We would not give relief for a voluntary escrow if we considered that a purpose of the company in requiring the escrow may be to construct a defence against a takeover.

17 In certain circumstances, an escrow employed as a defensive strategy or tactic may be subject to challenge before the court or the Takeovers Panel by a bidder, holder or us on the basis that it is

inconsistent with the duties of the target directors or constitutes unacceptable circumstances.

Underwriter escrow

Rationale

18 This relief would promote reorganisations by removing a disincentive for professional underwriters to underwrite. Entering into an underwriter escrow that restricts disposal of securities by a controller or substantial holder in a "sell-down" or "spin-off" transaction is unlikely to effect a change of control. It is unlikely that a company would use an underwriter escrow for defensive purposes or that an underwriter would use the escrow for control purposes. But a prolonged escrow may affect the market for control of the company. (We discuss our attitude to underwriting designed to avoid the purposes of Chapter 6 below: see topic I.)

19 Our proposed relief is limited to the period immediately following the public offering. Under our proposed relief, the underwriter escrow must be limited to 6 months after the transaction. This is the period often used in underwriter escrows. This period provides a balance between the following considerations:

(a) giving the underwriter a reasonable period to dispose of the shortfall; and

(b) minimising the period during which the controller or substantial holder is restrained from further selling. A prolonged escrow may affect the market for control over the company.

Commercial background

20 The underwriter's commercial motivation in requiring an escrow with the company's controller or substantial holder in a "sell-down" or "spin-off" transaction is to protect itself from a decrease in the price of securities that it may acquire in a shortfall under the public offering. Further selling by the controller may depress the price of the securities.

Substantial holding

21 We propose to give substantial holding relief for ASX escrow because there is an existing regime for disclosure concerning escrow in the Listing Rules. ASX requires pre-quotation disclosure of details of an escrow, continuous disclosure about the forthcoming release of securities from escrow and disclosure in the annual report: Listing Rules 3.10.5, 3.10A and 4.10.14 and ASX Guidance Note 11 *Restricted Securities* paragraphs 35–6.

22 In the case of voluntary escrow or underwriter escrow, while Listing Rules 3.10.5, 3.10A and 4.10.14 also apply, we will not give relief from the substantial holding requirements because these escrows are not mandatory and are not required to be in the form under Appendix 9A.

23 Substantial holding provisions require the company to disclose a substantial holding acquired through a voluntary or underwriter escrow, and any changes as securities are released from escrow: s671B. The company must also provide a copy of the agreement containing the escrow: s671B(4).

B Non-transferable securities

Policy proposal	Your feedback
Compulsory acquisition	
B1 We may give case-by-case relief modifying s661A(5) and 664A(4) to clarify that non-transferable securities under an employee incentive plan can be transferred under a compulsory acquisition notwithstanding any restraint in the constitution or terms of issue of the securities. We will also modify the procedure for completing a compulsory acquisition under Part 6A.3 of Chapter 6A.	**B1Q1** Should our relief be class order relief instead? **B1Q2** Instead should we give relief so that a holder of a non-transferable option under an employee incentive plan may forfeit or surrender their rights attaching to the option? **B1Q3** Should we give relief to treat non-transferable securities under an employee incentive plan as transferable in a *takeover bid or buy-out* as well as compulsory acquisition? **B1Q4** Are there any tax implications for employees that make our relief for takeovers or buy-outs unattractive? Tax implications would need to be fully resolved before we gave takeovers or buy-out relief. **B1Q5** If we were to give takeovers relief, should it apply only where the takeover bid is successful (eg where there is a 50.1% non-waivable minimum acceptance condition)? **B1Q6** Should we instead give relief to exclude non-transferable securities under an employee incentive plan from the 90% and 75% compulsory acquisition tests in s661A(1)(b)?

Explanation

Rationale

1 A bidder or 90% holder should not be prevented from acquiring 100% ownership of a company merely because securities under an employee incentive plan are non-transferable. The Explanatory Memorandum to the CLERP Bill paragraph 7.8 stated:

> "Compulsory acquisition of each class of securities can be difficult …where there are restrictions on transferring some securities (for example, securities issued under employee share schemes)."

2 Compulsory acquisition processes should be as similar as is practicable as between non-transferable and other securities.

3 Our proposed relief counters the possible defensive effect of non-transferable securities. Uncertainty whether the bidder can compulsorily acquire the securities may discourage bids. Many bidders seek 100% ownership of the target. In addition, non-transferable securities may constitute multiple small classes, which may complicate the bid and tend to entrench a minority.

Corporations Act provisions

4 We consider our proposed relief is appropriate because of indications that the compulsory acquisition provisions were intended to cover non-transferable securities:

(a) the definition of "convertible securities" in s9 states that: "An option may be a convertible security even if it is non-renounceable". The language "non-renounceable", suggests that the definition covers non-transferable options. Takeover bids, compulsory acquisitions and buy-outs extend to "convertible securities";

(b) the compulsory acquisition provisions "apply despite anything in the constitution of the company": s661A(5) and 664A(4). Although this will not apply directly where securities are non-transferable because of the terms of issue (including the rules of the employee incentive plan) rather than the constitution; and

(c) the Explanatory Memorandum to the CLERP Bill suggests that Chapter 6A was intended to cover non-transferable securities: see paragraph 1 of this topic.

5 We propose to modify s661A(5) and 664A(4), which state that the compulsory acquisition provisions have effect despite anything in the

constitution of the company. We would insert reference to the terms of issue as well as the constitution.. We would also modify Part 6A.3 of Chapter 6A, which provides for the transfer of the securities to the bidder or 90% holder as part of the completion of the compulsory acquisition.

Employee incentive plans

6 Employee incentive plans seek to align the interests of employees with those of the company. Non-transferable securities issued under a plan prevent employees from taking profits immediately and reinforce the interdependence of the company and the employee. The terms of an employee incentive plan may provide for the removal of restraints on transfer in the case of a compulsory acquisition, but many plans do not.

Classes

7 A non-transferable security will be in a different class to other securities if it "differs sufficiently in respect of rights, benefits, disabilities, or other incidents, as to make it distinguishable from any other category of shares": *Clements Marshall Consolidated Ltd v ENT Ltd* (1988) 13 ACLR 90, 93: see also topic D.

8 In the case of a share that differs from ordinary shares only because of its non-transferability, it is most likely that the share is in a different class if the constitution or terms of issue of the share provide that the share is non-transferable. In this case, it is clear the disability of non-transferability is "attached" to the share.

9 The security will not be in a separate class if it is non-transferable only because in the case of an employee it is subject to a trust. In this case non-transferability is not a disability attached to the shares but to the employee. In some plans, shares are purchased on-market and transferred to employees under the plan (see also paragraph 24 of this topic).

10 We do not consider that our relief making non-transferable securities transferable would have the effect of merging two classes (eg a class of non-transferable shares with ordinary shares). Our relief does not amend the constitution or terms of issue. It merely allows bidders and holders to transfer securities in particular circumstances irrespective of the constitution or terms of issue.

Forfeiture procedure

11 Bidders and 90% holders have sought from holders of non-transferable options the surrender or forfeiture of the holder's rights

attaching to the options in return for compensation as an alternative to a transfer of the options ("forfeiture procedure").

12 Under the forfeiture procedure, the bidder or 90% holder would then seek cancellation of the options by the company. An option is merely a contract: *Green v Crusader Oil NL* (1985) 10 ACLR 120. In cancelling an option (as opposed to a share), the target is not subject to capital maintenance requirements. The target and the non-transferable option holder can agree to vary or cancel their contract.

13 As an alternative to relief making non-transferable securities transferable, an option could be to give relief to facilitate this forfeiture procedure. Relief would be necessary because Chapter 6A assumes that the bidder or 90% holder will "acquire", "buy" and take a "transfer" of options. This language may not extend to the forfeiture procedure.

Buy-outs

14 A bidder or 100% holder must offer to buy-out securities, including non-transferable securities, under the buy-out requirements in Divisions 2 and 3 of Part 6A.1 and Division 2 of Part 6A.2. An option would be to give relief clarifying that holders may transfer non-transferable securities in a buy-out. But see tax implications at paragraph 21 of this topic. We would not give this relief unless the tax implications were fully resolved.

15 The rationale for this relief would be that holders of non-transferable securities should not be restrained from disposing of their securities in a buy-out merely because their securities are non-transferable. There may be significant disadvantages in being left as a minority holder. Inequality between holders of non-transferable securities and other holders should be minimised.

16 The obligation on a bidder to buy-out minority holders applies to "securities that are convertible into bid class securities": s663A(1). A non-transferable share will often convert into an ordinary share after a certain period. This may be an indication that the buy-out provisions were intended to cover non-transferable securities.

Takeovers

17 Another option may be to extend the relief so that non-transferable securities under an employee incentive scheme are transferable under a takeover bid.

18 This would allow holders of non-transferable securities to choose whether to accept a takeover bid, like other holders. But see tax

implications at paragraph 21 of this topic. We would not give this relief unless the tax implications were fully resolved.

19 Where the non-transferable securities constitute a separate class, the bidder cannot compulsorily acquire the non-transferable securities under s661A unless it can make an offer for them under a takeover bid and meet the 90% and 75% tests in s661A(1)(b). Although the bidder could compulsorily acquire the non-transferable securities under s664A(2) without making a bid for them. Under that subsection, a person can compulsorily acquire securities if:

(a) the securities are shares or convertible into shares; and

(b) the person's voting power in the company is at least 90%; and

(c) the person holds full beneficial interests in at least 90% by value of all the securities of the company that are either shares or convertible into shares.

20 It would be a requirement of our relief that the bid is subject to a 50.1% non-waivable minimum acceptance condition. Our relief would apply only where the bid is successful because a change in control (as opposed to the mere making of a bid) is an event justifying the release of an employee from restraints on transfer.

Tax

21 Although ASIC has no role in administering the Income Tax Assessment Act 1936 (ITAA 1936) and provides no advice on the operation of ITAA 1936, we note that tax implications may arise for employees from the forfeiture, takeovers and buy-out options for relief discussed above. This may make takeovers or buy-outs relief unattractive.

22 Division 13A ITAA 1936 provides income tax concessions in respect of shares or rights to acquire shares, obtained at a discount under an employee share scheme. ASIC relief may have implications for conditions of that relief, eg that the scheme was operated so that no recipient would be permitted to dispose of an employee share within 3 years of acquiring it: s139CE(3)(a) ITAA 1936.

23 These implications do not arise for our proposed compulsory acquisition relief. The conditions in s139CE of the ITAA 1936 are not breached because the disposal by the employee is compulsory by operation of the Corporations Act.

Securities held in trust

24 Securities under an employee incentive plan are often non-transferable because they are held in trust.

25 In a compulsory acquisition the securities will be transferred irrespective of the terms of the trust under the procedure for transfer in s666B. Our relief is not necessary.

26 If we were to give relief to treat non-transferable securities as transferable under a takeover bid or buy-out, this would not extend to securities in trust. We would not use our exemption and modification powers to require the trustee to release the securities from trust inconsistent with the terms of the trust if the holder accepts the offer, even if this were clearly within our powers.

C Exercise of convertible securities acquired under bid

Policy proposal	Your feedback
C1 We propose to give case-by-case relief to a bidder from the takeovers prohibition in s606 for an acquisition of voting shares by the bidder that results directly from exercise of convertible securities acquired under an off-market bid for the convertible securities.	
C2 The following requirements would apply to our proposed relief: (a) the bidder makes a takeover bid for all voting shares in the bid class (a full bid); (b) the bid for the convertible securities is subject to a non-waivable condition that the bid for the shares is: (i) unconditional; or (ii) subject only to conditions relating to either or both of the prescribed circumstances in s652C(1) or (2) and the condition in s625(3); (c) the bidder sends its first offers to holders under the bids for the convertible securities and for voting shares on the same day; (d) the bidder's statement discloses that the bidder has received our relief together with a brief description of the terms of the relief; (e) the bidder discloses its intentions	**C2Q1** Should we require that the bid for the shares extend to all shares issued on exercise of the convertible securities? **C2Q2** Should we require that the bid for the convertible securities is a bid for all convertible securities in the bid class (full bid)? **C2Q3** Should we require the bidder to make a bid for all the convertible securities in the company? **C2Q4** Should we require that the bids for the convertible securities and for voting shares end on the same day? **C2Q5** Should the bidder instead be required to disclose its intentions concerning exercise of the convertible securities only after it has acquired a significant proportion of the convertible securities? **C2Q6** Should the bidder instead be required to exercise all the convertible securities that it acquires under its bid?

Policy proposal

concerning exercise of convertible securities in its bidder's statement.

(e) the bidder exercises the convertible securities within 1 month after the end of the offer period.

C3 Before we give relief, the bidder must demonstrate that the offer under the bid for the convertible securities is comparable with and equitably related to the offer for the voting shares. An offer for convertible securities that is disproportionate by a significant margin compared to the offer for the shares is not equitably related. This assessment would be based on a valuation of the bid class convertible securities and the voting shares and any scrip consideration.

C4 Where the convertible securities and shares are quoted, we would compare the offer price to the market price.

Your feedback

C2Q7 Is a period longer than 1 month for the bidder to exercise convertible securities more appropriate (eg 2 months)?

C3Q1 Should our relief apply only where the bidder offers cash consideration (or a cash alternative) under its bids for both the convertible securities and the voting shares? The assessment whether the offers for convertible securities and shares are equitably related is more certain where the offers are for cash.

C3Q2 Should we give guidance on the method of valuing the convertible securities for the purpose of assessing whether the offers are equitably related? If so, how should the convertible securities be valued?

C3Q3 Should we assess the offers only by comparing the offer price for the convertible securities to the difference between the offer price for the shares and the exercise price for the convertible securities? This would be as an alternative to an option pricing model such as Black-Scholes.

C3Q4 In this context, is it appropriate to discount the time value of the convertible securities? Should our relief exclude an offer reflecting the time value? Should our relief exclude a scrip offer of convertible securities for convertible securities? Offering convertible securities would effectively reflect time value.

Policy proposal	Your feedback
	C3Q5 Should our relief be limited to quoted convertible securities? The valuation of quoted securities by reference to the market price is more transparent. A wider spread of convertible security holders is also more likely for quoted convertible securities, so that there is reduced risk that the bidder is targeting particular shareholders who are also convertible security holders.
C5 Ordinarily, we would expect that the bidder appoint an independent expert to report on the value and equity of the different offers. Alternatively, we may require an analysis of the value and equity of the different offers from the bidder's financial adviser.	**C5Q1** Should we ordinarily require an expert?
C6 We would not give this relief unless the bidder applies for it in good time before the date that it sends its offers to holders.	
C7 We would normally consult with the target before giving this relief.	

Explanation

Rationale

1 A bidder making a full, unconditional bid for voting shares in a company should be allowed to acquire all other securities: item 3 of s611.

2 Unlike before the CLERP Act commenced, bidders may make concurrent takeover bids for voting shares and convertible securities without our relief. The Corporations Act expressly recognises that the bidder may make "simultaneous takeover bids for different classes of securities in the target": s623(3)(c). The Explanatory Memorandum to the CLERP Bill in the context of s617(2) indicated that a purpose of the reforms is to better facilitate the acquisition of all securities in the target: "the [old] provisions limit[ed] a bidder to making a takeover bid for the shares in the bid class–that is, not including securities convertible into the bid class".

3 Where a bidder acquires convertible securities under a takeover bid, it should not be prevented by s606 from converting or exercising the convertible securities and acquiring the underlying voting shares. A prohibition on exercise may be a disincentive for bidders to bid for convertible securities. If the bidder were to acquire the convertible securities under a bid, it may be forced to sell or let them expire.

4 If bidders are discouraged from making a bid for convertible securities, convertible security holders seeking to access the benefits of the bid will be forced to pay the exercise price, await issue of the shares and accept the takeover bid.

5 Our proposed relief is consistent with the exemption for acquisitions of voting shares on exercise of convertible securities bought on-market: item 3 of s611. Acquisitions of convertible securities under a takeover bid are at least as well-regulated, transparent and equitable as on-market acquisitions: *Re Pinnacle VRB Ltd (No. 3)* (2001) 37 ACSR 346, 353.

6 Holders and the market should be informed about the treatment of convertible securities under the bid, and the bidder's intentions concerning exercise: s602(a).

Buying convertible securities on-market

7 Item 3 of s611 provides an exemption from the takeovers prohibition in s606 for voting shares acquired on the exercise of rights attached to convertible securities. (We have also given technical relief from item 3:

see [PS 171.50] and Class Order [CO 01/1542].) Under item 3, the bidder must have acquired a relevant interest in the convertible securities through an on-market transaction during a full, unconditional bid.

8 Similar requirements to those in item 3 would apply to our proposed relief for acquisitions of voting shares as a result of exercise of convertible securities acquired under a bid for convertible securities.

Requirements of relief

Full bid for shares

9 We are proposing as a requirement of our relief that the bidder has made a bid for all the voting shares in the bid class (ie a full bid). This is consistent with item 3(c) of s611.

10 The requirement follows from the policy that a bidder who has made a full, unconditional bid for the voting shares should be allowed to acquire all other securities in the company. It also means that control of the company does not pass through a bid for convertible securities without holders of voting shares having the opportunity to have all their shares acquired by the bidder.

Shares issued on exercise

11 The question arises whether we should require that the bidder's offer for the shares extend to shares that come to be in the bid class during the offer period due to a conversion or exercise of the convertible securities. We do not propose to require this because:

(a) under s617(2) a bid *may extend to* shares that come into the bid class–the subsection is permissive not mandatory; and

(b) item 3(c) of s611 does not require that the bid extends to later issued shares. The language "all the voting shares in the bid class" means instead a full, rather than proporational bid–see topic F.

Unconditional bid for shares

12 We are proposing as a requirement of our relief that the bid for the convertible securities is subject to a non-waivable condition that the bid for the shares is:

(a) unconditional; or

(b) subject only to conditions relating to either or both of the prescribed circumstances in s652C(1) or (2) and the condition in s625(3).

13 If the announced shares bid was not unconditional (except for prescribed circumstances conditions and the condition in s625(3)), the bidder must declare it unconditional if this convertible securities bid condition is to be fulfilled.

14 Under s650F(1)(b) the bidder may waive a condition of the bid for the shares only if it does so not less than 7 days before the end of the offer period. This means that where the bidder waives conditions of the share bid so that the bid for the convertible securities proceeds, shareholders will have at least a week to accept the offer for the shares.

15 This is consistent with item 3(d) of s611, which requires that the share bid is unconditional (except for prescribed circumstances conditions and the condition in s625(3)) at the time the bidder acquires the convertible securities on-market. We equate the time that the bidder declares its bid for the convertible securities unconditional with the time that a bidder "acquires" convertible securities on-market under item 3.

16 This requirement follows from the policies behind item 3 of s611 discussed in paragraph 10 of this topic, in particular giving shareholders the guaranteed opportunity to have their shares acquired by the bidder where control may pass through a bid for convertible securities.

Simultaneous offers

17 We are proposing as a requirement of our relief that the bidder sends its first offers to holders under the bids for the convertible securities and for the voting shares on the same day. This is similar to the requirement in item 3(b) of s611 that shares are acquired during the bid period.

Offer equitably related to offer for shares

18 An important requirement that we are proposing for our relief is that the offer under the bid for convertible securities must be equitably related to the offer under the bid for voting shares. Assessing whether the offers are equitably related would involve a valuation of the convertible securities, the shares and scrip consideration. If the offer for the convertible securities is disproportionate:

(a) there is a risk that the bidder is targeting shareholders who are also convertible security holders with a collateral benefit: s623; and

(b) the bidder may acquire a key parcel of voting shares on exercise of convertible securities having paid consideration significantly in excess of the value of the convertible security.

Market price

19 Where the convertible securities or shares or both are quoted, we will compare the offers to the market price in assessing whether the offers are equitably related. This is analogous to the requirement in item 3(b) of s611 that the bidder acquired the convertible securities through an "on-market transaction". Under this item, the bidder must acquire the convertible securities in the ordinary course of trading, in the case of ASX through a normal SEATS trade or certain crossings: see "on-market" definitions in s9 of the Act and in the ASX Business Rules. This on-market requirement ensures that the bidder acquires the convertible securities at a price that reflects the open market and does not reflect any pre-arrangement. (The on-market requirement also limits the risk that the bidder can direct the benefit of purchasing convertible securities to particular shareholders who are also convertible security holders, consistent with the collateral benefit prohibition: s623.)

Disclosure about our relief

20 The bidder should apply for this relief in good time before the date that it announces its bid. The bidder should not refer in its announcement to a defeating condition that we give this relief unless it has discussed the relief with us first.

21 It would be a requirement of our proposed relief that the bidder discloses in the bidder's statement it sends to holders that we have given relief together with a brief description of the terms of the relief. Other than in exceptional circumstances, we will not give this relief after the bidder has sent its offers to holders.

22 Holders and the market should know whether the bidder can exercise the convertible securities at the time the bidder makes its offers.

Bidder's intentions concerning exercise

23 We propose that the bidder must disclose its intentions concerning exercise of convertible securities in its bidder's statement.

24 Consistent with our Policy Statement 25 *Takeovers: false and misleading statements* [PS 25]:

(a) the bidder may reserve the right to depart from its statement of intentions about the convertible securities by attaching to it a clear, express qualification; and

(b) if the bidder changes its mind, it must immediately update the statement of its intentions in a supplementary bidder's statement.

The bidder should set out its intentions in the case of particular contingencies (eg various levels of acceptances for the convertible securities and shares).

Exercise all convertible securities

25 Another option would be to require the bidder to exercise all convertible securities acquired under its bid. We do not propose to require this because:

(a) it is not a requirement under the Act, although the Act clearly contemplates bids for convertible securities;

(b) it is not a requirement of item 3 that the bidder exercises all convertible securities that it acquired on-market; and

(c) it is the nature of convertible securities that a holder has the choice whether to exercise them. This is the right that the bidder acquires under a bid for convertible securities.

Exercise within 1 month after bid

26 It would be a requirement of our proposed relief that the bidder exercises the convertible securities within 1 month of the end of the offer period. This is so the bidder's holding of voting shares and level of control over the company crystallises without undue delay. Uncertainty about control of the company is not prolonged and the bidder does not surprise other holders with the timing of its acquisition of voting shares. The 1 month time limit corresponds with the time limit for dispatch of compulsory acquisition notices by the bidder under s661B(2)(a)(i), as a post-bid milestone.

Renounceable rights

27 We would also consider applications for relief so that a bidder may exercise renounceable rights acquired under a general offer comparable to a takeover bid. It is doubtful that rights are "securities" to which Chapters 6 to 6C apply under s92(3). Our relief would require that the offer for the rights complies as far as practicable with Chapters 6 and 6C as if the offer were a takeover bid.

28 Issues raised by the Takeovers Panel matters in the MatlinPatterson Global Opportunities Partners LP bid for renounceable rights and shares in Anaconda Nickel Ltd may be relevant to such an application.

D Classes of securities

Note: The proposals in this topic would amend topic C of IPS 159.

Policy proposal	Your feedback
Relief to merge classes	
D1 We will give case-by-case relief to allow two or more classes of securities to be treated as the same class in a bid only where the value of offers for each class is clearly: (a) ascertainable; and (b) equitable in view of the values of the different securities.	
D2 This will be clearest where an equitable cash adjustment is made to the price offered for the different classes.	
D3 We may require an analysis of the value of the different securities and the value and equity of the different offers from the bidder's financial adviser and consult with the target. We may require the bidder to appoint an independent expert to verify the value and equity of the different offers (see D5 and D8).	
Options	
D4 An example of this relief is that we may give case-by-case relief to treat different series of options as the same class where the terms of the options are identical, except for exercise prices and exercise dates.	
D5 Ordinarily, we would expect that the bidder appoint an independent expert	**D5Q1** Should we ordinarily require the appointment of an expert?

Policy proposal	Your feedback
to value the different series of options.	**D5Q2** Should we give guidance on the valuation of the options? Is an option pricing model like Black-Scholes the preferred method in the context of a bid?
Partly-paid securities	
D6 Fully and partly-paid securities are in the same class where voting and dividend rights attaching to partly-paid securities are full or proportional to the amounts paid up: s605(2).	**D6Q1** Can holders be unfairly advantaged or prejudiced because partly-paid securities are in the same class as fully-paid securities? How may this affect the course of the bid and any compulsory acquisition?
D7 Where partly-paid securities are in the same class as fully-paid securities, a bidder can offer a kind of consideration for partly-paid securities different to that offered for fully-paid securities. The different kind of consideration must be attributable to the fact the offer relates to securities on which different amounts are paid up or remain unpaid: s619(2). The kind of consideration must reflect the value and commercial characteristics of the partly-paid securities.	**D6Q2** If partly-paid securities were in a different class to fully-paid securities, would this have a defensive effect or tend to entrench minority holders?
	D6Q3 Should we give relief so that partly-paid and fully-paid securities are in the same class, to remove doubt? This relief would be on the basis that the offers for each class are equitable: see proposal D1.
D8 Ordinarily, we would expect that the bidder appoint an independent expert to value the partly-paid securities.	**D6Q4** Should we give guidance on the valuation of partly-paid securities for the purpose of assessing the value and equity of the offers for partly-paid and fully-paid securities? If so, how should partly-paid securities be valued?
	D6Q5 Should we ordinarily require an expert to value the partly-paid securities?

Explanation

Classes under a bid

1 Subsection 605(1) provides that a takeover bid can be made for securities within a particular class. A bid must relate to securities in a class of securities: s617. A bidder who wishes to bid for two or more classes may concurrently undertake two or more separate bids. All offers must be the same, except that differences in the offers attributable to the fact the offers relate to securities on which different amounts are paid up or remain unpaid may be disregarded: s619(2)(c).

Relief to merge classes

2 Interim Policy Statement 159 [IPS 159.11] provides for relief to merge classes where "there can be an equitable cash adjustment to the price offered for the different classes". We propose to amend this policy because the language "cash adjustment" has the potential to cause confusion where the bidder is offering different classes of scrip consideration for different classes of securities. We are also proposing to amend [IPS 159] to make it clear that bidders may offer different kinds of consideration for partly-paid and fully-paid securities: see paragraph 10 of this topic.

Valuing options

3 Our proposed relief to treat different series of options as the same class involves a valuation of the options as a basis for assessing the equity of the different offers for the different series of options. Our proposed relief allowing a bidder to exercise convertible securities acquired under a takeover bid also discusses the valuation of convertible securities: see policy proposal C3.

Partly-paid securities

Rationale

4 As far as is practicable, holders of partly-paid securities should have a reasonable and equal opportunity to participate with holders of fully-paid securities in the benefits accruing through a bid: s602(c) and 605(2). The consideration that the bidder offers for partly-paid securities must be equitably related to the consideration that it offers for fully-paid securities: see also policy proposal C3. This means that differences in consideration that the bidder offers to partly-paid holders must be attributable to differences in amounts paid up: s619(2)(b).

Corporations Act provisions

5 Subsection 605(2) provides that "securities are not taken to be different classes merely because:

(a) some of the securities are fully-paid and others are partly-paid; or

(b) different amounts are paid up or remain unpaid on the securities".

6 We consider that s605(2) will not operate in all cases to treat partly-paid and fully-paid securities as being in the same class. It will not cover partly-paid securities carrying no dividend or voting rights.

Legislative background

7 Subsection 605(2) is based on the Legal Committee of the Companies and Securities Advisory Committee (now CAMAC) *Anomalies Report* (March 1994) Recommendation 26. The Legal Committee commented:

> "The Corporations Law should provide that partly-paid and fully-paid shares are not, for that reason alone, separate classes of shares for the purpose of Chapter 6. Where there are other differences, for example, partly-paid shares having reduced rights not proportional to the amount paid up, common law principles would determine whether there are separate classes."

This supports our view that partly-paid securities with full or proportional rights are in the same class as fully-paid securities.

General law

8 The position at general law was different to that under s605(2). At general law a "class" was held to mean:

> "…a category of shares which differs sufficiently in respect of rights, benefits, disabilities or other incidents, as to make it distinguishable from any other category of shares.": *Clements Marshall Consolidation Ltd v ENT Ltd* (1988) 13 ACLR 90, 93.

In *Clements Marshall*, partly-paid shares held by employees were in a different class to fully-paid securities because the partly-paid securities had different voting rights, dividend rights and liability to calls.

Partly-paid securities with full voting and dividend rights

9 Our position that partly-paid securities are in the same class as fully-paid securities is not entirely free from doubt. There is an argument that under s605(2) only partly-paid securities that have full voting and

dividend rights are in the same class as fully-paid securities. According to this interpretation, s605(2) does not apply to partly-paid securities with proportional rights because they are not in a different class "merely because [they are] partly-paid". They are in a different class because they have different (although proportional) voting and dividend rights. This would read down the operation of s605(2), minimising its effect on the general law position. Many partly-paid securities have proportional rights.

Different kinds of consideration

10 Where partly-paid securities are in the same class as fully-paid securities, a bidder may offer a different kind of consideration for partly-paid securities if the difference is attributable to (correlates with, is caused by or is commensurate with) the fact that the offers relate to securities on which different amounts are paid up or remain unpaid: s619(2) and *Taipan Resources NL (No. 10)* Unreported (23 May 2001) and *Taipan Resources NL (No. 11)* Unreported (26 June 2001). The type of consideration must reflect the value and commercial characteristics of the partly-paid securities. In *Taipan* the bidder offered options for partly-paid securities that were out of the money.

E Compulsory acquisition: exercised options

Policy proposal	Your feedback
E1 We may give case-by-case relief for a bidder from the 75% compulsory acquisition test in s661A(1)(b)(ii) where the bidder offered to buy convertible securities under its bid. Under our proposed relief, convertible securities that are exercised or converted from the date set by the bidder under s633(2) to the end of the offer period would be excluded from the number of convertible securities that the bidder offered to acquire under the bid.	**E1Q1** Is it appropriate instead to treat a convertible security that is exercised as a rejection of the bidder's offer for the convertible securities?

Explanation

Rationale

1 The 75% test in s661A(1)(b)(ii) is a test whether holders overwhelmingly accepted the offer under the takeover bid. If a holder converts or exercises its convertible security rather than accepting the offer for the convertible security under the bid, the holder will neither have accepted nor directly rejected the bidder's offer for the convertible securities. Convertible securities that are converted or exercised should be excluded from the test.

75% test

2 The 75% test is one limb of the test for compulsory acquisition following a bid. The bidder may compulsorily acquire any securities in the bid class if during, or at the end of the bid, the bidder and their associates have acquired at least 75% (by number) of the securities that the bidder offered to acquire under the bid: s661A(1)(b)(ii). Convertible securities converted or exercised will not be counted as securities acquired by the bidder (the numerator in the percentage calculation). But, without our relief, these convertible securities will be counted as securities that the bidder offered to acquire (the denominator).

3 Holders may convert or exercise their convertible securities after the bidder has determined to whom it must send its offers for convertible securities, usually to accept the bidder's offer for ordinary shares. The bidder's offer for ordinary shares may extend to shares that come into existence during the period from the date set by the bidder under s633(2) to the end of the offer period following conversion or exercise of convertible securities: s617(2) and Class Order [CO 01/1543]. (The date under s633(2) is the date for determining to whom offers will be sent. It must be between the date that the bidder serves the bidder's statement on the target and the date of the first offer: s633(3).)

4 If a substantial proportion of holders convert or exercise their convertible securities after the offer under the bid, it may be impossible for the bidder to meet the 75% test.

F Compulsory acquisition: full bid– s661A(1)

Policy proposal	Your feedback
F1 We propose to interpret s661A(a)(i), which states that for the bidder to compulsorily acquire the bid must have been to "acquire all the securities in the bid class", as a requirement that the bid was full, not proportional.	**F1Q1** Does the language "all the securities in the bid class" instead mean the bidder must bid for all bid class securities issued up to the end of the offer period? **F1Q2** Should we give class order relief to remove any doubt?
F2 The language "all the securities in the bid class" does not mean the bidder must have bid for all possible bid class securities, ie those issued up to the end of the offer period. The same language is used in s618 to refer to a full, not proportional, bid.	

Explanation

Rationale

1 A bidder may compulsorily acquire following an off-market bid only if it made a full bid. This is because a bidder seeking to maximise its chance of obtaining 100% should not make a proportional bid. Section 661A assists bidders seeking 100% ownership of the target, while balancing the interests of minority holders.

2 To compulsorily acquire, the bidder and its associates must have acquired at least 75% (by number) of the securities that the bidder offered to acquire under the bid: see Policy Statement 171 *Anomalies and issues in the takeover provisions* at [PS 171.148] and Class Order [CO 01/1544]. The bidder may compulsorily acquire securities in the bid class only if the bidder's offer under its bid received overwhelming acceptance.

3 This test of overwhelming acceptance would be imperfect in the case of a proportional bid. The bidder must give holders the opportunity to accept into the bid for their entire existing parcel of bid class securities.

Corporations Act provisions

4 To compulsorily acquire bid class securities under s661A following an off-market bid, the bidder must have made a bid for "all the securities in the bid class". This language has caused some confusion. Some bidders have suggested that the bidder must have bid for all possible bid class securities, including those issued during the offer period. A takeover bid must relate to existing securities under s617(1), but may extend to securities issued up to the end of the offer period on exercise of convertible securities under s617(2).

5 We disagree with this interpretation.

6 Under s618(1) an "offer for securities under an off-market bid must be an offer to buy:

(a) all the securities in the bid class; or

(b) a specified proportion of the securities".

The language "all the securities in the bid class" in s618(1)(a) is identical to the language in s661A(1). The language means a full, not proportional, bid.

7 If the language in s618 covered securities issued during the offer period due to the exercise of convertible securities, this would mean that under s618 the bidder must offer to acquire these later issued

securities. This would be inconsistent with the permissive language in s617(2). Under s617(2), the bid "may extend" to later issued securities. That s617(2) refers to *extending* a bid to later issued securities reinforces the idea that an ordinary full bid is an offer for existing securities.

8 If the bidder were required to bid for later issued securities as a precondition to compulsory acquisition under s661A, this would indicate a policy that all holders must receive an offer under the bid before their securities can be compulsorily acquired. But the bidder may elect to compulsorily acquire securities issued after the offer period: s661A(4)(b)–(d). The bidder cannot offer to acquire these securities under its bid.

G Holders aware of information– s636(1)(m)

Policy proposal	Your feedback
G1 For the purposes of s636(1)(m), the bidder can treat information as having been disclosed to holders only if: (a) the information has already been sent to the holders; or (b) the information has been so widely and accurately reported that it is likely all holders are aware of it. **G2** Normally, the bidder must not omit material information required under s636(1)(m) from the bidder's statement merely because the information has been previously disclosed to a market operator or ASIC.	

Explanation

1 Subsection 636(1) states that the bidder does not have to disclose information under s636(1)(m) "if it would be unreasonable to require the bidder to do so because the information had previously been disclosed to the holders". Paragraph 636(1)(m) is a general bidder's statement content requirement: the bidder must disclose any other information that is material to the making of the decision by a holder whether to accept an offer under the bid.

Newpapers

2 A bidder can omit from its bidder's statement information published in newspapers as having been previously disclosed to holders only if it is so widely and accurately reported that it is probable all target holders are aware of the information: *ICAL Ltd v County NatWest Securities Aust Ltd* (1988) 13 ACLR 129 and *Pancontinental Mining Ltd v Goldfields Ltd* (1995) 16 ACSR 463.

Information notified to market operator

3 The same test applies to information notified to a market operator or lodged with ASIC. Such information is not normally so widely reported that all target holders are aware of it.

General

4 This policy would supersede Practice Note 66 *Transaction specific prospectuses* at [PN 66.60]–[PN 66.63].

H Consent to use statement: officials and publications

Policy proposal	Your feedback
H1 We propose to give class order relief modifying s636(3) and 638(5) so that the bidder's or target's statement may include a statement by a person without the person's consent and without stating that the person has given their consent. Our relief would allow the inclusion of a statement that: (a) fairly represents a statement by an official person; (b) is a correct and fair copy of, or extract from, a public official document; or (c) is a correct and fair copy of, or extract from, a statement that: (i) has already been published in a book, journal or comparable publication; and (ii) was not made in connection with the takeover bid or any person, business or property the subject of the bidder's or target's statement.	

Explanation

Rationale

1 A bidder or target should obtain the consent of the person who makes a statement before using it so that the person can:

(a) control or limit their liability; and

(b) control the overall effect of the statement.

2 A bidder or target may, in some cases, best discharge their obligation to provide all information material to the decision whether to accept an offer under a bid by including a statement that is not specific to the bidder, target or bid.

3 It is generally impractical, impossible or disproportionately expensive for the bidder or target to obtain the consent of the author of such a statement in a book, journal or other comparable publication to comply with s636(3) or 638(5).

4 It is less critical that an official person can control and limit liability for their statement because of the special position of the Crown in an action for misleading or deceptive conduct: see paragraph 8 of this topic.

Publications

5 Case law indicates that in general the author of a statement will not be civilly liable for the inclusion in a prospectus of that statement (or a statement based on it) if the original statement was not made for the purpose of being included in the prospectus: *Morgan Crucible Co plc v Hill Samuel Bank Ltd* [1991] 1 All ER 148, *Bride as Trustees for the Pinwernying Family Trust v KMG Hungerfords* (1991) 109 FLR 256 and *Esanda Finance Corporation Ltd v Peat Marwick Hungerfords (Reg)* (1997) 142 ALR 750.

6 The phrase "book, journal *or comparable publication*" includes reference to statements in a form and of a standard similar to that normally contained in a book or journal, but made available through the internet. This excludes, for example, references to statements made in internet chat rooms, newsgroups and home pages with unaccountable content (with anonymous participants or without editorial control).

Government official

7 Without our relief bidders or targets would be required to obtain consent to refer to statements of government officials and government

publications (eg the Australian Bureau of Statistics, the Commonwealth Bureau of Meteorology and their publications).

8 With respect to the position of the Crown in an action for misleading or deceptive statements in a takeover document, we note that:

(a) Chapters 6–6D bind the Crown in right of the Commonwealth and do not bind the Crown in right of any State–s5A(3); and

(b) nothing in the Corporations Act makes the Crown in any right liable to a pecuniary penalty or to be prosecuted for an offence–s5A(5).

9 Guidance as to the meaning of the phrase "public official document" can be found in cases that have considered the term "public document" in an evidentiary context. A "public document" is one made by a public official as a result of a public inquiry and available to the public: Lord Blackburn in *Sturla v Freccia* [1874-80] All ER Rep 657. Accordingly, documents do not become "public official documents"merely because they have been lodged with a government department or statutory authority and are maintained for public access on a registry by the department or authority.

General

10 Our relief would not protect a bidder or target that uses the statement from liability if the statement is presented in a misleading or deceptive manner.

11 Our proposal on s636(3) and 638(5) seeks to achieve consistency with our policy on the equivalent fundraising provision: s716(2), see Practice Note 55 *Prospectuses–citing experts and statement of interests* [PN 55] and Class Order [CO 00/193].

12 We currently give this relief case-by-case: see Policy Statement 171 *Anomalies and issues in the takeover provisions* at [PS 171.139]. We may give other relief from the requirement of consent to use statements under s636(3) and 638(5): see [PS 171.133].

I Rights issue underwriting–s611 item 10

Policy proposal	Your feedback
I1 We propose to continue our policy in NCSC Policy Statement 112 of carefully considering any rights issue falling within the terms of the exemption in item 10 of s611 that appears to be designed to avoid the purpose, spirit or intent of Chapter 6: see s602. For example, a rights issue may be structured so that control of a company may pass to underwriters or sub-underwriters of the rights issue without a takeover bid.	**I1Q1** Are there any factors suggesting whether a rights issue is an abuse of item 10 of s611 not mentioned in this topic? **I1Q2** Are there any other particular examples of transactions falling within the terms of an exemption in s611 and designed to avoid the purpose of Chapter 6 that we should address at this time?
I2 A person who abuses the rights issue exemption in item 10 risks an application to the Takeovers Panel by us or another party for a declaration of unacceptable circumstances.	
I3 We will normally closely examine a proposed rights issue underwritten by a person who already controls or is likely after the rights issue to emerge with control of the company.	
I4 Where holders have approved acquisitions by the underwriter as a result of shortfalls under item 7 of s611, we would not normally have cause to examine the matter.	

Explanation

Rationale

1 Any arrangement that falls within the terms of the exemptions in s611 to the takeover prohibition, but is designed to avoid the intent of Chapter 6 risks an application to the Takeovers Panel for a declaration of unacceptable circumstances by us or another party.

2 A transaction designed to give control to the underwriter that is presented to the holders and market as a rights issue may offend the purposes in s602.

3 In this case:

(a) holders and the market are not fully informed about the acquisition of control by the underwriter; and

(b) holders may not have a reasonable or equal opportunity to participate in the benefits accruing through a proposal under which the underwriter acquires a substantial interest in the company.

Item 10 of s611

4 Item 10 of s611 provides an exemption to the takeovers prohibition in s606 for rights issues. The exemption expressly extends to an acquisition by a person as underwriter or sub-underwriter to the rights issue.

5 The exemption covering acquisitions by an underwriter is designed to allow for the possibility that a bona fide rights issue may fail to attract a large number of subscriptions, leaving an underwriter with an obligation to take up the shortfall.

6 A substantial shortfall in a rights issue may have many causes. An obvious one is where a major holder controls a substantial percentage of the capital and does not take up its entitlement.

7 The underwriter or sub-underwriter may emerge with control of the company either solely as a result of the shortfall or as a result of the shortfall and previous purchases. The underwriter may increase its voting power past 20% of the company. An underwriter that holds more than 20% voting power in a company may increase its holding by more than the 3% allowed under the creep exemption: item 9 of s611.

Relevant factors

8 Objective factors may suggest whether a purpose of the rights issue is to give control to the underwriter. In examining a rights issue we may have regard to matters such as:

(a) the pricing of the rights issue. Pricing above the current market price is more likely to lead to a substantial shortfall;

(b) the financial situation of the company. For example, if the company is financially distressed, it will have an urgent and compelling need for fresh capital and will be less likely to find an underwriter that is not an associate (see paragraph 9 of this topic);

(c) the ratio of the rights issue. The larger the number of new shares for old, the more dilutive the rights issue. A high ratio may suggest an abuse of item 10;

(d) the purpose of the rights issue. If the company cannot clearly identify a need for the capital, this may suggest an abuse of item 10;

(e) the shareholding structure of the company and the response of major shareholders to the issue;

(f) the terms of the underwriting;

(g) whether holders have been advised of the identities of sub-underwriters;

(h) dealings by the underwriter or sub-underwriter (or an associate) in shares of the company before or during the rights issue;

(i) dealings by the underwriter or sub-underwriter (or an associate) in the rights. Acquisitions of rights may suggest the underwriter is seeking control;

(j) any associations between the underwriter or sub-underwriter and one or more substantial holders or a group of substantial holders;

(k) any role of the underwriter or sub-underwriter in the making of the issue and its influence on the affairs of the company; and

(l) whether the underwriter or sub-underwriter is associated with the company's directors.

Controller as underwriter

9 We realise that circumstances may sometimes be such that:

(a) the company has a compelling need for a capital injection;

(b) the most favourable means of raising the funds is through a rights issue; and

(c) the success of the issue without considerable shortfalls may not be assured.

In these circumstances persons who already control or are likely after the rights issue to emerge with control of the company should not necessarily be precluded from underwriting or sub-underwriting the issue.

10 We will normally closely examine a rights issue under these circumstances.

Holder approval

11 Where holders have approved acquisitions by the underwriter as a result of shortfalls under item 7 of s611, we would not normally have cause to examine the matter.

12 In addition, where the underwriter is related to the company, the underwriting may need approval by shareholders as a related party transaction under Part 2E.2: see MR 00/425 "ASIC acts on related party underwriting". Note that an entity is a related party if the entity believes or has reasonable grounds to believe that it is likely to become a related party at any time in the future: s228(6).

Unacceptable circumstances

13 The Takeovers Panel may declare circumstances to be unacceptable whether or not the circumstances constitute a contravention of the Corporations Act: see s 657A(1). It may declare that a rights issue constitutes unacceptable circumstances although it falls within the terms of item 10 of s611.

General

14 An underwriting under item 13 of s611 may raise similar issues.

15 We consider other aspects of the underwriting exemptions under items 10 and 13 in Policy Statement 61 *Underwriting–application of exemptions* [PS 61].

16 This policy replaces NCSC Policy Statement 112 *Arrangements contrary to the purpose of the Takeovers Code s60.*

J Changes to a bidder's statement between lodgment and dispatch

Note: The proposals in this topic would amend topic F of IPS 159.

Policy proposal	Your feedback
J1 We propose to interpret s637(2) as requiring a replacement bidder's statement under our Class Order [CO 00/344] to be dated with the date on which the replacement was lodged with us. It should not be dated with the date that the original bidder's statement was lodged.	
J2 The replacement bidder's statement should: (a) explain that it replaces the original bidder's statement lodged with us; and (b) give the date that the original bidder's statement was lodged.	

Explanation

1 Where a supplementary bidder's statement is lodged before dispatch of the bidder's statement, we have given relief to allow a bidder to dispatch a replacement bidder's statement (which includes the changes made in the supplementary bidder's statement) instead of:

(a) where the bid class securities are quoted–the original bidder's statement (see item 6 of s633(1) and item 6 of s635); and

(b) where the bid class securities are not quoted–the original bidder's statement and the supplementary bidder's statement: see IPS 159.29, item 6 of s633(1), s635, 647(3)(c) and Class Order [CO 00/344].

K Approval of notices of variation

Note: The proposals in this topic would amend topic N of IPS 159.

Policy proposal	Your feedback
K1 We propose to adjust our relief. We will no longer give relief for an agent authorised by each director to sign a notice of variation. This is unnecessary because under our relief the focus is on approval of the notice of variation rather than signing it. This is consistent with s637. The signature that appears on the variation is governed by s351. **K2** We will continue to give case-by-case relief so that a notice of variation under s650D can be approved in any of the ways a bidder's statement can be approved under s637. **Lodging with ASIC: s351** **K3** As with the bidder's statement, a notice of variation lodged with us must still comply with s351. It must still be signed by a director or secretary of the company. If it is a foreign company, it may be signed by: (a) its local agent; or (b) if the local agent is a company–a director or secretary of the company: s351(1). Our relief does not affect the requirement in s351. We do not have a power to give relief from this requirement.	

Explanation

Notice of variation signed: s650D(3)

1 Contrary to s637, without our relief a notice of variation to a bidder's statement under s650D must be *signed*:

(a) if the bidder is an individual–by the bidder;

(b) if the bidder is a body corporate with two or more directors–by at least two directors of the bidder who are authorised to do so by a resolution passed at a directors' meeting; or

(c) if the bidder has only one director–that director (s650D(3)).

Bidder's statement approval: s637

2 We propose to give relief allowing a notice of variation to be *approved* in any of the ways a bidder's statement can be approved under s637. Section 637 requires that the copy of the bidder's statement that is lodged with us must be *approved* by:

(a) for a bidder that is a body corporate:

(i) for cash consideration only–a resolution passed by the directors; or

(ii) otherwise–a unanimous resolution passed by all the directors; or

(b) for a bidder who is an individual–the bidder: s637(1).

This relief enables a notice of variation to be approved by way of circular resolution.

Our relief

3 Under current IPS 159 we may give relief so that instead of being signed by directors of the bidder, as required by s 650D(3), a notice of variation can be either:

(a) approved in any of the ways a bidder's statement can be approved under s637; or

(b) signed by an agent authorised by each director to execute a notice of variation: see [IPS 159.73].

4 We will remove the reference to a notice of variation being "*signed* by an agent authorised by each director to execute a notice of variation".

Development of policy proposal paper

We have developed this policy proposal paper in light of our experience of applications received by us and issues raised concerning Chapters 6 to 6C since March 2000. We have also considered:

(a) Explanatory Memoranda and draft Bills for the CLERP Act;

(b) Corporate Law Economic Reform Program Proposals for Reform: Paper No. 4 *Takeovers. Corporate control: a better environment for productive investment* (1997);

(c) Chapter 6 of the Corporations Law pre-CLERP Act;

(d) Legal Committee of the Companies and Securities Advisory Committee Report (now CAMAC) *Anomalies in the Takeovers Provisions of the Corporations Law* (1994);

(e) comments provided by the Takeovers Panel in response to informal consultation;

(f) comments provided by the ASX on escrows (topic A) in response to informal consultation;

(g) IPS 159 *Takeovers: discretionary powers* [IPS 159], as well as the following ASIC policies:

  (i) Policy Statement 25 *Takeovers: false and misleading statements* [PS 25];

  (ii) Policy Statement 49 *Employee share schemes* [PS 49];

  (iii) Policy Statement 61 *Underwriting–application of exemptions* [PS 61];

  (iv) Policy Statement 171 *Anomalies and issues in the takeover provisions* [PS 171];

  (v) NCSC Policy Statement 112 *Arrangements contrary to the purpose of the Takeovers Code s60*;

  (vi) Practice Note 55 *Prospectuses—citing experts and statement of interests* [PN 55];

  (vii) Practice Note 66 *Transaction specific prospectuses* [PN 66];

(h) ASX Listing Rules, particularly Chapter 9 Restricted Securities and ASX Guidance Note 11 *Restricted Securities and Voluntary Escrow*; and

(i) the following Takeovers Panel and court decisions:

(i) *Re Bigshop.com.au Ltd (No 2)* Unreported (2 November 2001);

(ii) *Bride as Trustees for the Pinwernying Family Trust v KMG Hungerfords* (1991) 109 FLR 256;

(iii) *Clements Marshall Consolidated Ltd v ENT Ltd* (1988) 13 ACLR 90;

(iv) *Esanda Finance Corporation Ltd v Peat Marwick Hungerfords (Reg)* (1997) 142 ALR 750;

(v) *ICAL Ltd v County NatWest Securities Aust Ltd* (1988) 13 ACLR 129;

(vi) *Kingston v Keprose Pty Ltd (No 2)* (1987) 12 ACLR 599;

(vii) *Morgan Crucible Co plc v Hill Samuel Bank Ltd* [1991] 1 All ER 148;

(viii) *Re Otter Gold NL & Australian Securities Commission* (1997) 15 ACLC 387;

(ix) *Pancontinental Mining Ltd v Goldfields Ltd* (1995) 16 ACSR 463;

(x) *Re Pinnacle VRB Ltd (No. 3)* (2001) 37 ACSR 346;

(xi) *Taipan Resources NL (No. 10)* Unreported (23 May 2001); and

(xii) *Taipan Resources NL (No. 11)* Unreported (26 June 2001).

Key terms

In this policy statement, a reference to:

"Act" means the *Corporations Act 2001*;

"ASX" means Australian Stock Exchange Ltd;

"ASX escrow" means restrictions on the disposal of securities, through a restriction agreement with the holder of restricted securities under Chapter 9 of the ASX Listing Rules;

"CLERP Act" means the *Corporate Law Economic Reform Program Act 1999*;

"IPS 159" means Interim Policy Statement 159 *Takeovers: Discretionary powers*;

"ITAA 1936" means the *Income Tax Assessment Act 1936*;

"s606" (for example) means a section of the Act;

"underwriter escrow" means an escrow that an underwriter requires a company's controller or substantial holder to enter into preventing further sales of shares by the controller; and

"voluntary escrow" means an escrow that is not an ASX escrow with a person to whom the company issues securities in return for services or assets.

Some expressions used in this policy proposal paper are defined in the Act.

What will happen next?

Stage 1

Thursday 20 February 2003	Our policy proposal paper released

Stage 2

Friday 4 April 2003	Comments due on our policy proposal
April–May 2003	Drafting of final Policy Statement 159

Stage 3

May 2003	Final Policy Statement 159 released

Your comments

You are invited to comment on the proposals and issues for consideration in this paper. All submissions will be treated as public documents unless you specifically request that we treat the whole or part of your submission as confidential.

Comments are due by Friday 4 April 2003 and should be sent to:

Andrew Fawcett, Senior Lawyer
Regulatory Policy Branch
Australian Securities & Investments Commission
GPO Box 5179AA
Melbourne VIC 3000
facsimile: 03 9280 3306
email: andrew.fawcett@asic.gov.au

You can also contact the ASIC Infoline on 1300 300 630 for information and assistance.