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Takeovers in Australia

2019

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Corporate/M&A – Australia
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Introduction

In Australia, takeovers of listed companies or unlisted companies with more than 50 shareholders are regulated. The most common structures to effect a takeover in Australia are off-market takeover bids and schemes of arrangement.

The main rules that govern takeovers in Australia are:

- Chapter 6 of the Corporations Act 2001 (Cth) (Corporations Act), which governs takeovers of Australian companies listed on the Australian Securities Exchange (ASX) or certain other Australian markets, or unlisted companies with more than 50 shareholders
- Chapter 5 of the Corporations Act, which provides an alternative means of effecting a takeover through a court approved scheme of arrangement
- the Foreign Acquisitions and Takeovers Act 1975 (Cth) (FATA), which regulates acquisitions of Australian businesses and assets by foreign investors
- for takeover of companies listed on the ASX, the ASX Listing Rules would also apply which set out some parameters around timetables and disclosure obligations, and
- the Competition and Consumer Act 2010 (Cth) (CCA) which prohibits certain mergers and acquisitions that are likely to have the effect of substantially lessening competition in a market in Australia.

Australian takeovers legislation has the objective of ensuring that takeovers in Australia are orderly and fair and that they occur in an efficient, competitive and informed market.

Application of Australian takeovers law

Australian takeovers legislation applies to takeovers of companies or other bodies corporate which are registered in Australia and are either listed on the ASX or certain other Australian markets, or have at least 50 shareholders. The takeovers law also applies to all listed Australian-registered managed investment schemes.

Takeover mechanisms

Takeovers can be achieved through a takeover bid (either off-market or on-market) but there are also a limited number of alternative mechanisms available for achieving a similar outcome.

The viability of using other mechanisms should always be considered before proceeding down the route of a takeover bid. These alternatives include:

This guide provides an overview of some of the key issues in acquisitions of control of public companies in Australia. We hope it will help you to better understand the regulatory framework governing the Australian M&A market.

For further information, please contact one of our team members listed at the back of this publication.

Takeover thresholds at a glance

Threshold	Description
0%	FIRB approval may be required for a foreign government investor if the acquisition gives the investor some special rights such as ability to appoint directors or asset managers.
5%	Acquirer required to give a "substantial holder notice" to the target company and the ASX. Ability to force the company to call a shareholders meeting and vote on certain matters (eg removal of directors).
10%	Acquisition of a "blocking stake" to prevent any other person from compulsorily acquiring 100% of the target following a takeover bid. If the acquirer is a foreign government investor, the investor may be required to seek prior approval from the Treasurer under the Australia's foreign investment rules.
15%	Shareholders' approval required if a listed company wishes to issue more than 15% of its issued capital during any 12 month period.
20%	**Takeovers law limitation** – A person may not acquire an interest of more than 20% in a company unless it makes a takeover bid to all shareholders or another exception applies. FIRB – Potential requirement for notice and prior approval under *Foreign Acquisition and Takeovers Act* (if bidder is a foreign person).
25%	Holder able to prevent special resolution being passed (eg a vote on a scheme of arrangement).
30%	If the bidder holds more than 30% of the target, the target company is required to commission an independent expert to prepare a report opining on whether the proposed acquisition transaction is fair and reasonable.
50%	Majority control of target. Majority holder able to ensure passing of ordinary resolution, including a resolution to replace the entire board of directors.
75%	Holder able to ensure passing of special resolution (eg to amend the constitution of the target).
80%	In the case of a scrip bid, capital gains tax relief could be available to the target shareholders if the bidder acquires 80% of the target
90%	Holder able to compulsorily acquire the remaining 10% of the shares.
100%	Bidder able to gain benefits of outright control (eg to access the target's cash flow).

Takeovers

Takeovers: Basic concepts

The 20% rule

The key rule for takeovers in Australia is that a person may not acquire a relevant interest in the voting shares of a company to which the takeovers law applies (see above), if the acquisition would result in the person having more than 20% voting power in the company, unless the acquisition is conducted through one or more exceptions or gateways outlined in Chapter 6 of the Corporations Act. The 20% threshold is defined very broadly under the Corporations Act, and captures for example, interests held by a person who is acting in concert with, or is otherwise an associate of, the acquirer.

At the basic level, this means an acquirer is subject to Australian takeovers regulations if it wants to acquire more than 20% of an Australian listed company or an unlisted company with more than 50 shareholders.

The two key concepts underpinning Australia's takeovers law are voting power and relevant interest.

What is "voting power"?

Voting power is defined as the total number of votes attached to all voting shares in which the acquirer and its associates have a relevant interest, divided by the total number of voting shares issued by the company.

What arrangements can give rise to a "relevant interest"?

Relevant interest is defined very broadly. A person will be deemed to have a relevant interest in a share of the company if that person:

- is the registered holder of the share
- has power to control the voting rights attached to the share
- has power to control the disposal of the share
- has entered into an agreement with another person with respect to the share and would have a relevant interest in the share if the agreement were performed (eg, entry into a share purchase agreement), or
- owns 20% of another entity which holds shares in the first mentioned company. The person is also deemed to have a relevant interest in shares in the downstream entities which the other entity controls.

Having some measure of control over the rights attached to voting shares is enough to create a relevant interest. It does not matter whether the power or control is express, implied, formal or informal or exercisable jointly or alone.

Who is an associate of the acquirer?

In calculating a person's voting power, the Corporations Act takes into account those voting shares in which an associate of the person has a relevant interest. Therefore the concept of an "associate" is critical in the application of takeovers law in Australia.

Associates can be broadly categorised in the following groups:

- **Corporate groups**: the Corporations Act provides that the associates of a body corporate include a body corporate it controls, a body corporate that controls it or a body corporate that is controlled by an entity that controls it. This means that an acquirer will not be able to avoid the application of the takeovers law by "splitting" its shareholding across different subsidiaries or related entities each holding less than 20% of the shares in the target.
- **Agreement relating to board composition or conduct of affairs**: a person is deemed to be an associate of another person if the two have, or propose to enter into, a relevant agreement for the purpose of controlling or influencing the composition of the relevant entity's board or the conduct of its affairs. The concept of "relevant agreement" is defined very broadly under the Corporations Act and includes any agreement, arrangement or understanding whether or not it is legally enforceable. The affairs of an entity include, among other things, ownership of shares in the body, exercise of the voting rights or control over the disposal of shares.
- **Persons acting in concert**: a person will be deemed to be an associate of the acquirer if the person is acting, or proposing to act, in concert with the acquirer in relation to the relevant entity's affairs. This may include two entities jointly approaching a shareholder with a view to acquiring the shares and splitting them following completion of the acquisition.

Case Study

In Ambassador Oil and Gas 01, the Takeovers Panel found that negotiations between the bidder (Drillsearch Energy Limited) and Mr Kleo Hatziladas and the directors of Ambassador, who controlled a significant shareholding in the target (Ambassador Oil and Gas Limited), in relation to 'acceptance statements' gave rise to an association under the Corporations Act, and therefore gave Drillsearch voting power in Mr Hatziladas's shares in breach of the takeovers law.

In making the finding, the Panel relied on some circumstantial evidence:

- the fact that Mr Hatziladas and the directors who made acceptance statements accepted the offer exceptionally early and virtually all at the same time which was uncommercial
- the manner in which the target directors "acquiesced" in the role played by Mr Hatziladas in organising for a further 19.9% of the shares in Ambassador to be acquired by Drillsearch from a number of other shareholders as a pre-bid stake, and
- the fact that Mr Hatziladas appears to have orchestrated these additional acquisitions.

This decision reminds bidders that they must carefully consider the manner in which they conduct pre-bid negotiations, especially in circumstances where one or two major shareholders have effective control of the target, or when seeking acceptance statements.

Norton Rose Fulbright acted for the successful applicant in this matter.

Key regulatory bodies

ASIC

All key takeover documents are required to be lodged with ASIC. ASIC has broad powers to exempt and modify the takeovers law. It is also the main body responsible for regulating and enforcing the takeovers law. ASIC has the power to refer matters to the Takeovers Panel.

Takeovers Panel

The Takeovers Panel is the main forum for resolving disputes in relation to takeover bids.

The members of the Panel are appointed from among takeover practitioners (eg lawyers, investment bankers, consultants, board directors, industry professionals and other mergers and acquisitions experts), who are called to adjudicate when required.

The Panel may make a declaration of "unacceptable circumstances", even in circumstances where there is no express breach of the takeovers law, on the application of ASIC or any person whose interests are affected by the circumstances. For example, the use of certain lock-up devices to defend against a takeover can give rise to unacceptable circumstances even though there is no express prohibition under the Corporations Act.

The Takeovers Panel can also review an ASIC decision to exempt or modify the takeovers law.

Norton Rose Fulbright acted for the successful applicant in this matter.

Off-market takeover bids

Off-market takeover bids have historically been the most commonly used method to acquire control of a listed company in Australia.

A bidder which publicly proposes to make a bid is required to proceed with the bid within 2 months of the date of the proposal. There is very little room for a company to reverse such an announcement once it is made.

The bidder prepares a bidder's statement (which includes an offer document that sets out the terms of the offer) which is sent to shareholders by mail. The target prepares a target's statement which is also mailed to shareholders and includes the target directors' recommendation. Shareholders then decide whether or not to accept the offer prior to the expiry date of the offer.

Bid Consideration

The consideration offered by the bidder to acquire shares in the target company may be in the form of cash, scrip or combination of both. There is no requirement that the offer consideration must be at a "market level", however:

- the consideration must be not less than the highest price at which target shares were acquired or agreed to be acquired by the bidder (or any of its associates) during the 4 months preceding the bid
- the target board is unlikely to recommend, and shareholders unlikely to accept, an offer which is too low, and
- if an independent expert's report is required or otherwise voluntarily commissioned by the target, the expert will opine on whether the consideration offered is fair and reasonable.

Disclosure documents

The main disclosure documents used in an off-market takeover bid are the bidder's statement and target's statement, both of which are regulated by Chapter 6 of the Corporations Act. We set out below the main content requirements:

Bidder's Statement	Target's Statement
• details of the bidder and its intentions regarding the target's business, assets and employees; • how the bidder will fund the cash consideration (if any) together with the details of any financing arrangements; • details of any collateral benefits given or any purchases of target shares by the bidder or its associates during the previous 4 months; and • any other information known to the bidder that is material to a target shareholder deciding whether to accept the offer.	• all the information that target shareholders and their professional advisers would reasonably require to make an informed assessment whether to accept the offer; • a recommendation (with accompanying reasons) by each director as to whether or not the bid should be accepted; and • if the bidder is a director (or a corporation that shares a common director with the target) or already has 30% voting power in the target, a report by an independent expert on whether the bid is fair and reasonable to shareholders not associated with the bidder.

The following factors should be considered in determining what information to include in a target's statement:

- What is the real value of the bid compared to the value of the target?
- Are the conditions attached fair and reasonable?
- Is the bid likely to be declared or become unconditional?
- Is the bid price fair and reasonable?
- What are the consequences for the target if the bidder gains control?
- Is it likely a higher bid will be made?
- What do the directors recommend?

A target board should also consider any conflicts of interest which any particular director has in relation to a transaction.

The Corporations Act contains detailed liability provisions to deal with misleading or deceptive statements or conduct in relation to takeover bids for both the bidder and the target company. For example, a bidder/target and its directors may be liable for a defective bidder's or target's statement and will be potentially liable to any person who suffers loss or damage as a result of a misleading or deceptive statement. For these reasons, both the bidder's statement and target's statement are often vetted through a process called verification, which is designed to ensure that each statement within the bidder's statement or target's statement is signed off by the relevant person (which may be the board, management, tax, financial or legal advisers).

Bid conditions

A key structuring benefit of using an off-market takeover bid is that an offer may be made conditional on the occurrence (or non-occurrence) of certain matters.

However, the combination of Corporations Act and guidance issued by the Takeovers Panel prohibits certain types of conditions, such as:

- maximum acceptance condition (eg the bidder will only acquire up to 51% of the shares)
- conditions that discriminate between individual shareholders
- conditions requiring payments to officers of the target company, and
- conditions which rely on the bidder's subjective opinion for fulfilment or are otherwise solely within the control of the bidder.

The bidder can elect to free its offers from any or all of the defeating conditions at any time during the offer period up to the final seven days of the offer period.

Common bid conditions

Minimum acceptance
Often between 50% to 90% allowing offers to be withdrawn unless the bidder is able to proceed to outright control or compulsory acquisition.

FIRB/ACCC
Receipt of all necessary regulatory approvals.

MAC
No material adverse change occurs or is announced.

Market movement
The relevant market index does not fall materially (eg 10%) during the bid period.

"Business as usual" condition
Restrictions on target increasing or reducing its share capital, or disposing of all or a substantial part of its business or assets.

Timetable

Unless the target company agrees otherwise, the bidder's statement under an off-market takeover bid may only be sent to the target shareholders within 14 to 28 days after the document is first sent to the target company. This gives the target company at least two weeks to review the bidder's statement and potentially take action in the Takeovers Panel if it forms the view that the bidder has not complied with relevant laws or policy (eg inadequate disclosure).

Once the bidder's statement is sent to target shareholders, off-market takeovers must remain open for a minimum of one month and may not exceed 12 months in duration.

Offers are automatically extended for another 14 days if during the final seven days of the offer period the offer consideration is improved, or the bidder reaches 50% voting power.

The target company has 15 days after the despatch of bidder's statement to prepare and issue its target's statement. Although ASIC has power to extend this period, it rarely does so.

A "friendly" off-market takeover bid usually takes around two to three months to complete.

A typical timeline for an off-market takeover bid is set out below.

Getting to 90% and acceptance facilities

For most bidders, the end goal of an off-market takeover bid is to acquire 100% of the target company. Under Australian takeovers law, acquisition of 100% of the target shareholding is only assured after the bidder acquires at least 90% which would allow it to compulsorily acquire the minority shareholding under the compulsory acquisition provisions of the Corporations Act. For these reasons, off-market takeover bids sometimes include a minimum acceptance condition of 90%.

This creates a 'catch 22' situation: a lot of institutional investors will not accept into a takeover bid until the bid has been declared unconditional. However, without the support of the institutional investors, the bidder is unlikely to reach the 90% threshold to allow it to declare the bid unconditional. To deal with this issue, the Australian market has developed two tools:

(a) instead of making an off-market takeover bid, to structure the takeover by way of a scheme of arrangement, which provides an "all-or-nothing" outcome for the bidder. See further information on schemes (from page 16), or

(b) use of an institutional acceptance facility (IAF) to allow the institutions to provide guidance to the bidder on whether or not they intend to accept the takeover bid should the bid be declared unconditional.

An IAF allows institutional shareholders to provide acceptance instructions to a third party trustee, who will typically hold the instructions but not action them until the bid is declared unconditional by the bidder. Until the trigger event, institutional shareholders have full flexibility to retract their instruction at any time. From a bidder's perspective, it will have the benefit of knowing the level of acceptances that it will receive should the bid be declared unconditional.

Issues relevant to an off-market takeover bid

Truth in takeovers

In accordance with its "Truth in Takeovers" policy, ASIC monitors the conduct of market participants (bidders, targets and substantial shareholders) making public statements leading up to and during a takeover bid. In particular, a statement made by a market participant that they will or will not do something in the course of the bid acts like a contract. If a market participant wants to reserve the right to depart from its statement (for example, on the happening of some event) it must clearly qualify the statement. For example, a bidder cannot publicly make the following statements and then depart from them:

- This offer is final/this is our last offer.
- The consideration payable for the takeover bid will not be increased.
- The offer period will not be extended.

To prevent or minimise the likelihood that a misleading or deceptive statement might be made which could adversely affect the outcome of an offer, a bidder should ensure that only officers who have knowledge of these regulations and are authorised to speak about the offer make any public statements about the takeover or the target and that before making or publishing any public statement appropriate legal and financial advice is obtained.

No escalators

A bidder cannot enter into an agreement that promises to pay to a shareholder an amount that is based on the offer price under the takeover bid eg any increase in the takeover bid offer price (although all shareholders who accept a takeover bid will receive the highest bid price).

No collateral benefit

A bidder must not during the offer period for a takeover give a benefit to a shareholder if the benefit is likely to induce the shareholder to accept the bidder's offer, if the benefit is not offered to all of the other shareholders. Examples of prohibited collateral benefits would include offering finance to a shareholder, purchasing from or selling assets to a shareholder and offering the shareholder termination benefits in relation to their employment with the target that they would not otherwise be entitled to.

Funding

A bidder must have a reasonable basis for believing that it will have the necessary funds available to pay the maximum consideration payable to accepting shareholders (assuming 100% acceptance) by the time its offer becomes unconditional.

The Panel requires that at the time of announcing a proposed bid, a bidder at least have sufficient cash reserves available or a sufficient commitment from a financier in place. Definitive documentation with a financier (at least a binding term sheet) should be completed and signed before offers are sent to target shareholders.

Negotiations with target company

A bidder may require a target to commit to exclusivity arrangements in order to proceed with its proposal. The most common types of deal protection or "lock-up" devices are break fees and no-shop agreements.

Bidders in "friendly" bids also often require the directors of the target to publicly support the bid. Any agreement to do so must always expressly allow the directors to withdraw their support should their duties as directors require them to do so (for example, if a higher bid is made), although this would usually trigger payment of a break fee.

Negotiations with target shareholders

Bidders should exercise care in negotiating pre-bid agreements with substantial shareholders. In particular, no agreement to acquire shares representing more than 20% of the voting shares in the target can be reached, as this would give the bidder a relevant interest in those shares.

It is acceptable to discuss the price to be paid for shares if a takeover bid is launched, provided no agreement or understanding results. It is not acceptable for the bidder to extract an undertaking that the shareholder would deal exclusively with the bidder regarding more than 20% of the shares in the target as this would give the bidder a degree of control over the shares and would constitute a relevant interest.

In addition, the Takeovers Panel has recently issued a new Guidance Note 23 in relation to statements of intention made by target shareholders in the context of a control transaction. The Takeovers Panel has confirmed that a statement made by a target shareholder that it intends to accept or reject the bid may give rise to unacceptable circumstances in certain circumstances. Therefore bidders should tread carefully when seeking statements of support from target shareholders.

On-market takeovers

An on-market takeover bid allows the bidder to acquire shares in the subject of the takeover directly on market. An on-market bid can be implemented in a very short period of time: within an hour after announcement of the bid, the bidder is able to start acquiring shares on market.

However, on-market bids are not used very often in Australia for this reason: the bid must be in cash and unconditional from day one. Acquisitions of shares on market by the bidder cannot be reversed, so there is a real risk that the bidder may be left with a shareholding at the end of the bid period that is not sufficient to deliver control of the target company to the bidder.

In Australia, there are only on average three to five on-market takeover bids per year. The vast majority of them are for transactions below $50m.

The largest on-market takeover bids over the past decade include BG's successful $5.3 billion bid for Queensland Gas Company in 2008 and the $275m unsuccessful bid by Gujarat NRE Coking Coal for Jindal Steel & Power in 2013.

In BG's on-market bid for Queensland Gas Company, BG acquired control of the target within a week, and reached the 90% compulsory acquisition threshold in three weeks.

What is the advantage of an on-market bid?

The greatest advantage of an on-market bid from the perspective of a bidder is timing: once the bid is announced on the ASX, the bidder is free almost immediately to start purchasing shares on-market in excess of the 20% threshold. This places a lot of pressure on the target directors, who then only have 15 days to prepare and despatch the target's statement.

By comparison, a bidder under an off-market takeover bid has to wait at least 14 days after announcement (unless the target company agrees to shorten the time period) before it is allowed to send the bidder's statement to the target shareholders and start acquiring shares pursuant to the bid. The target company then has a further 15 day period to prepare and despatch the target's statement in response.

Another advantage of an on-market takeover bid is that the bidder may increase the bid price through the offer period without having to pay a higher price to shareholders who have already sold their shares into the bid.

On-market bids must be unconditional

One of the biggest limitations and reasons why on-market bids are not used often in Australia is because any such bid must be unconditional from the outset. This means the bid cannot be subject to a minimum acceptance condition, and any regulatory approvals required (such as FIRB or competition clearance) must be obtained prior to launching the bid. The inability to include a minimum acceptance condition means that there is a real risk the bidder may be left with a non-controlling stake in the target company if it is unsuccessful in its bid.

Bidders in an on-market bid have some very limited protection from the list of "prescribed occurrences" as set out in the Corporations Act (such as target company issuing shares, or an insolvency event occurs in respect of the target). On the occurrence of any such event, the bidder may withdraw unaccepted offers made under an on-market bid, but only if the bidder's voting power at the time is at or below 50%.

Schemes of arrangement

As an alternative to a takeover bid, a court approved scheme of arrangement may be used to acquire control of an Australian company in certain circumstances. This may be done through a restructure of the company's share capital primarily by transferring all or a specified proportion of each shareholder's securities to a bidder or cancelling existing securities (except those held by the bidder). Over the past decade, schemes of arrangement have become as common as takeover bids as a means of effecting a change of control in Australia.

In practice, schemes are only used where the takeover is 'friendly'. It can achieve a range of outcomes and is a more certain process (both for timing and outcome, but not necessarily success) than a takeover. However, a scheme is not as flexible as a takeover bid in effecting changes to the offer terms and timetable, which are often essential in a competitive bid situation.

Advantages of a scheme

'All or nothing' outcome

Unlike a takeover bid, a scheme will produce an 'all or nothing' outcome. To successfully implement a scheme, a resolution in favour of the scheme must be passed at meetings of each class of the shareholders of the target, by:

- more than 50% (by number) of the shareholders of the target present and voting either in person or by proxy (the "headcount test"), and
- at least 75% of the votes cast on the resolution (the "special resolution" test).

In each case, excluding any votes cast by the bidder or its associates. If the scheme is not approved by the requisite majorities at the shareholders' meeting, then the bidder will not acquire any interest in the shares of the target company.

Flexibility

As a scheme of arrangement is designed to cater for various company restructures, it has the advantage of being more flexible in structuring an acquisition transaction compared to a takeover bid. Not only can a bidder include a combination of cash and scrip in the scheme (as in a takeover), the bidder can also incorporate an asset transfer, divestment, reduction of capital, special dividend payment by the target and other transactions to be implemented simultaneously with, and conditional on the approval of, the control transaction.

Co-operation of the target

In comparison to a takeover bid process which is controlled by the bidder, a scheme of arrangement is proposed by the target company to its shareholders. This means that schemes are only used in a friendly transaction, with the co-operation of the target board. It is possible for a bidder to use 'bear hugs' or apply other commercial pressure to publicly propose a scheme deal to the target company, but the relevant provisions of the Corporations Act dealing with schemes of arrangement still require the target company (and not the bidder) to drive the scheme process and prepare and despatch the scheme booklet to shareholders.

Basic steps in a scheme of arrangement

The basic steps in the scheme process are as follows:

1	The target and the bidder negotiate the terms of the scheme and the scheme implementation agreement (referred to below). The scheme implementation agreement sets out the terms of the acquisition of the target by the bidder.
2	Once the scheme implementation agreement is signed, the scheme is announced and the bidder and the target and their respective advisers prepare the scheme booklet to be sent to target shareholders in connection with the scheme meeting. The scheme booklet must include the disclosures required by the Corporations Act including the directors' recommendations and any other material information. Invariably, an independent expert's report is obtained.
3	The scheme documentation is lodged with ASIC for review. The review period is usually 14 days.
4	Following the ASIC review, the target aplies to the court for orders convening the scheme meeting. This is usually an ex-parte application but the court will allow objectors with an obvious interest to be heard at the first court hearing. There is then a 28 day notice period prior to the scheme meeting.
5	If the scheme is approved by the requisite majorities at the scheme meeting, the target returns to the court for an order approving the scheme.

6	At the second court hearing, the court primarily will look at whether the requirements of the Corporations Act have been complied with and whether the scheme involves any unfairness or lack of good faith. A court will be reluctant to impose its own commercial judgement in relation to a scheme particularly where it has been approved by an overwhelming majority of shareholders of the target.
7	Once approved by the court, the scheme takes effect upon lodgement of the court order with ASIC.

Court approval

One factor which could restrict the use of a scheme as a means of achieving a corporate acquisition is section 411(17) of the Corporations Act.

In broad terms, section 411(17) precludes the court from approving a scheme unless either:

- the court is satisfied that the purpose of the scheme was not to avoid the takeover provisions of the Corporations Act, or
- ASIC issues a statement that it has no objection to the scheme. The practice of ASIC is that it will issue a letter, shortly after the shareholder meeting, stating that it has no objection to the scheme. The letter is issued if, at that time, ASIC is satisfied that shareholders have received all material information that they need to make an informed decision, they have received reasonable and equal opportunity to share in the benefits provided under the scheme, and the shareholder meetings were properly conducted.

ASIC is largely indifferent as to whether a change of control is effected through a takeover bid or a scheme of arrangement, but it requires that parties proposing a scheme substantively comply with the disclosure obligations and structural requirements of the takeover provisions in Chapter 6 of the Corporations Act (*ASIC Regulatory Guide 9*). ASIC has used section 411(17) as a means to oppose the convening of shareholder meetings to consider a scheme if the protections for target shareholders in Chapter 6 are compromised by a proposed scheme.

To date, section 411(17) has generally not proved to be a practical impediment to a change of control proceeding by way of a scheme rather than a takeover bid.

Classes of shareholders

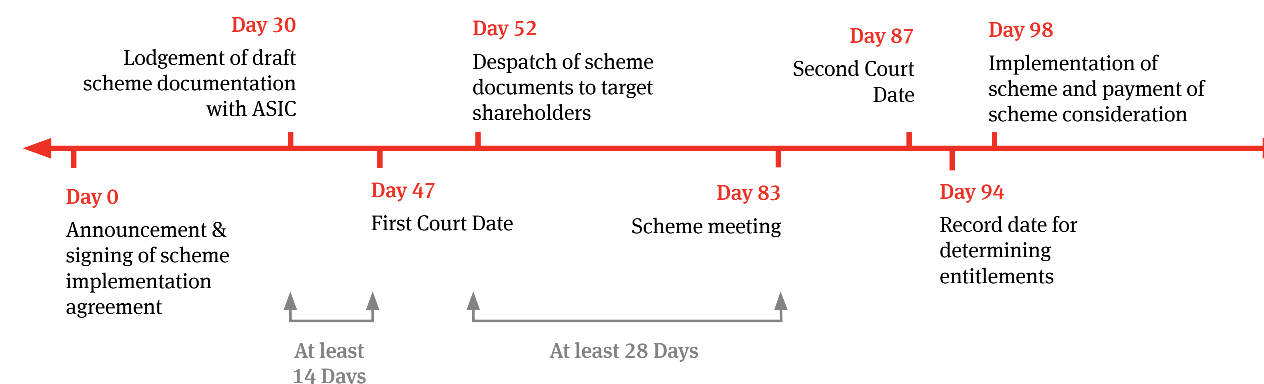
One of the most difficult issues that arises in schemes is the consideration of share classes and whether or not the shareholders with the right to vote on a scheme should do so at separate class meetings. If there is more than one class of members, there must be a separate meeting of, and an affirmative vote that satisfies the voting thresholds from, the relevant class in order for the members of that class to be bound by the proposed scheme.

The mere fact that a shareholder receives some benefit from the overall proposal that other shareholders do not receive does not automatically mean that the shareholder constitutes a separate class. The focus of the test is on whether the legal rights of the shareholders are so dissimilar that they should constitute a separate class for voting on the scheme.

Some examples of shareholders that may be classified in a different class for the purposes of a scheme of arrangement include:

- a shareholder who will receive a collateral benefit (considered on a “net benefits” test) that will not be available to other shareholders in the company; and
- a shareholder who is also a creditor whose rights as a creditor may be materially affected by the implementation of the scheme.

Indicative timetable



A scheme is implemented under a different timetable compared to a takeover bid, given the additional documentation required for the court process, the holding of the court hearings and convening the shareholders’ meeting. It is common for a scheme to take around four months to proceed from execution of an implementation agreement between the bidder and target to final approval and implementation.

There is often very little difference in timing between a recommended takeover bid and a scheme. However, with a scheme the implementation date is usually more certain and can be determined from the outset.

Comparison between takeovers and schemes

Both off-market takeovers and schemes of arrangement are used extensively for control transactions in Australia. There are some statistics suggesting that schemes are now used more often than takeovers for friendly transactions, which may be due to a number of factors:

- Schemes give the bidder certainty of outcome. The scheme resolutions will either be approved at the meeting (in which case the bidder will acquire 100% of the target), or rejected at the meeting (in which case the bidder will not acquire any shares). This is particularly important when the bidder requires acquisition financing to fund its bid. The financiers will generally only agree to fund when there is certainty that the bidder will acquire 100% of the target company.
- Schemes are subject to fewer specific rules and are therefore a more flexible structure than takeover bids. For example, related transactions (such as sale of assets or a reorganisation) can be built into the scheme for approval as part of one transaction, whereas takeover bids are generally implemented in isolation.
- Schemes can be implemented with approval from holders of 75% of the shares present and voting at the scheme meeting (provided the headcount test is met), whereas takeover bids require acceptances from 90% of the shares the subject of the bid if the bidder is to be able to compulsorily acquire outstanding shares and move to 100% ownership.

The table below sets out, at a high-level, the key differences between schemes and takeover bids:

	Off-market takeover	On-market takeover	Scheme of arrangement
Approval threshold	Compulsory acquisition only triggered at 90% Shareholders who do not act (ie accept) are not counted towards the 90%		Lower approval threshold (75% by shares and 50% by number of shareholders)
Certainty of result	The 90% acceptance condition is frequently waived. Bidder can end up with less than 100%	Must be unconditional	All-or-nothing
Blocking stake	10.1% sufficient to block compulsory acquisition.		25% required. However, if 60-80% voter turnout, 15-20% could block.
Regulatory risk	Can be subject to regulatory conditions. Subject to ASIC and Takeovers Panel	Must be unconditional Can therefore end up with less than 50.1% Subject to ASIC and Takeovers Panel	Subject to ASIC and court review
Flexibility to increase price	Bidder can vary the terms of the offer Any variation will apply to all shareholders	Bidder can vary the bid consideration Any variation will only apply to future on-market trades	Less flexible as the scheme cannot include terms which allow for unilateral variation Variation will usually require court consent
Timetable	Usually 7-12 weeks plus 5 weeks compulsory acquisition. Can be up to 12 months	Can be faster – bids can be accepted immediately after announcement	Can be a fixed timetable, often 12-15 weeks
Control of process	Largely driven by the bidder		Largely driven by the target

Alternative structures

Alternative structures for acquiring control

The following are some of the other ways (apart from takeover bids and schemes of arrangement) to acquire control of a company:

Shareholder approval in general meeting	Shareholders can give their approval in general meeting to a person acquiring a relevant interest that would otherwise contravene the 20% rule. The notice of meeting must be accompanied by all information known to the bidder and the target material to the decision on how to vote on the matter. An ordinary resolution approving the acquisition is required. Interested parties cannot vote. Usually, a report by an independent expert will be commissioned to provide shareholders with impartial and expert information on the proposal. In effect, shareholders can agree to an acquisition of control without receiving a takeover offer for their own shares. The acquisition can be effected by a transfer of existing shares or an issue of new shares.
3% creeping acquisition	A shareholder can increase its holding in the target company by up to 3% every six months without making a takeover bid. This allows a patient shareholder gradually to increase its holding without launching a bid for the remaining shares. Once a shareholder has had a voting interest of at least 19% for an entire six month period it may acquire shares that increase its voting power by a further 3% in each succeeding six month period. Depending on the circumstances, a major shareholder may be satisfied with gradually increasing its shareholding in the target using the 3% creep. However, care must be taken in applying the 3% creep, as the calculation can be affected by other factors, such as movements in issued capital and the holdings of associates.
Acquisition pursuant to a rights issue	A shareholder may increase its voting interest in the company beyond the 20% takeover threshold through the acquisition of shares under a pro rata rights issue. The voting power of a participating shareholder to a rights issue may increase, for example, if other shareholders decide not to participate in or only partially participate in the rights issue. The exception also extends to underwriters and sub-underwriters of a rights issue. However, the Takeovers Panel and ASIC have issued guidance on how a rights issue should be structured so as to avoid it being used as a tool by a major shareholder to acquire control of the company. In summary, the target company is required to take all reasonable steps to mitigate any control effects that may result from the proposed rights issue. Some of the issues discussed in the Takeovers Panel guidance note include pricing, size, renounceability and underwriting arrangements with an existing shareholder.
Reduction of capital/share buy-backs	It is possible for an existing shareholder to acquire control of a company through a selective capital reduction or share buy-back by the company, resulting in the shareholder holding all or majority of the outstanding shares in the company. Under the Corporations Act, a capital reduction or share buy-back must not be proposed if it will materially prejudice the company's ability to pay its creditors. The process and documentation for a selective capital reduction or share buy-back is similar to that of a scheme of arrangement, ie requiring the company to convene a shareholders' meeting to consider the proposal, which requires approval from 75% of the votes cast at the meeting. However, no court approval is required.

Competition issues

Anti-trust and merger control regulations

Section 50 of the *Competition and Consumer Act 2010* (Cth) prohibits takeovers or mergers that would have the effect, or be likely to have the effect, of substantially lessening competition in a market. Section 50(3) provides a non-exhaustive list of the factors to be taken into account when assessing whether a takeover or merger would be likely to substantially lessen competition.

Voluntary merger clearance regime

There is no formal requirement in Australia for the notification of a proposed aquisition or merger[1]. However, it is recommended by the Australian Competition and Consumer Commission (ACCC) that transactions are notified to the ACCC for review in advance of completion of the transaction where both of the following apply:

- the products of the parties are either substitutes or complements, and
- the merged firm will have a post-merger market share of greater than 20% in the relevant market(s).

Where Foreign Investment Review Board (FIRB) approval is required, FIRB will consult with the ACCC on any potential competition issues arising from the proposed transaction. FIRB will not approve a proposed transaction until the ACCC has advised that the merger or acquisition will not be likely to result in a substantial lessening of competition in any relevant market in Australia. For this reason, even where the above thresholds are not reached, approaching the ACCC may be appropriate.

Clearance of a proposed merger or acquisition can be achieved by an informal clearance process or authorisation of the transaction by the ACCC or declaration by the Federal Court that the transaction does not substantially less competition.

The informal clearance process is the avenue most commonly used by merger parties as it allows for flexibility and negotiation with the ACCC on any perceived competition issues. This process also enables parties to make a confidential submission on the proposed transaction.

For proposed transactions unlikely to present any material competition issues, informal clearance may be obtained within a 'pre-assessment' period of approximately 2-4 weeks.

For proposed transactions where further consideration of the potential competition implications is required, the ACCC carries out a public review process to assess the extent of competition concerns over a period of approximately 8 to 12 weeks (subject to any further extensions of the timeline proposed by the ACCC due to potential issues or further information requirements). At the completion of this process, the ACCC will release a final decision that the merger or acquisition is unlikely to result in a substantial lessening of competition or it will release a Statement of Issues indicating that there are competition concerns.

A Statement of Issues will commence a Phase II assessment of a further 8 to 12 weeks. At the completion of a Phase II assessment, the ACCC will release its decision on whether it will allow the transaction to proceed, or it would seek to intervene should the parties seek to complete the transaction. The ACCC may also accept remedies from the merger parties to alleviate any competition concerns.

Should authorisation of transaction be sought from the ACCC, this is a public process subject to a statutory 90 day assessment period (with extension of the timeline by agreement). Authorisation will be granted where the ACCC is satisfied that the proposed acquisition would not be likely to substantially lessen competition, or the likely public benefit from the proposed acquisition outweighs the likely public detriment, including any lessening of competition.

Other considerations

Certain markets may be of interest to the ACCC even where the transaction does not trigger the ACCC's notification thresholds. The ACCC will unilaterally commence a review of a proposed transaction where it is in an industry of interest.

The structure of a transaction should be considered against competition clearance risk. Where the proposed transaction has the potential to raise competition clearance concerns, consideration should be given to whether competition clearance should be a condition precedent to completion.

Where the transaction is global, the likely interplay of global antitrust regulators is a key timing consideration, and the structure of the transaction may need to contemplate clearance being granted at different times across jurisdictions.

1 An acquisition includes asset or share acquisitions, options on assets or shares, an indirect acquisition, the creation of a joint venture, a majority shareholding in a competitor, a minority shareholding where the acquirer obtains veto rights, and pre-emptive rights.

Takeovers in Australia

Remedies and sanctions

Since notification is voluntary, there are no penalties for failure to notify a transaction. However, where the ACCC forms the view that a merger or acquisition is likely to contravene Section 50, it may apply to the Federal Court to grant injunctions, declare a merger or acquisition void, accept an undertaking and/or impose a penalty for a contravention of up to the greatest of:

- A$10 million for companies (up to A$500,000 for individuals)
- three times the value of the benefit the company obtained directly or indirectly and that is reasonably attributable to the contravening conduct, and
- 10% of the annual turnover of the company and all its subsidiaries (if any).

Foreign investment regulations

Foreign investment framework

The Australian Government's approach to foreign investment is to encourage foreign investment consistent with community interests. Investment proposals by foreign investors which may result in an interest being acquired in Australian companies are regulated by the Foreign Acquisitions and Takeovers Act 1975 (Cth) (FATA) and associated regulations. The FATA is administered by the Treasurer, on the advice of the Foreign Investment Review Board (FIRB). The Treasurer has the power to prohibit certain foreign investments if they are considered 'contrary to the national interest' having regard to the widely held community concerns of Australians.

> Statistically, Australia's record in approving foreign investments remains one of the best in developed nations with less than 0.1% of the applications received by the Foreign Investment Review Board (FIRB) rejected each year.
>
> Since 2001, less than ten significant business acquisition applications have been rejected by the Australian Government.

Significant actions and notifiable actions

The FATA categorises transactions which are subject to Australia's foreign investment framework into two broad groups – significant actions and notifiable actions.

Significant actions

Significant actions are transactions which trigger the power of the Federal Treasurer to make certain orders under the FATA. Notification to the Treasurer of significant actions is voluntary (except where the action is also a notifiable action – discussed below). Significant actions include:

- the acquisition of interests in Australian entities or businesses, or their assets
- the acquisition of interests in Australian land
- the acquisition of a direct interest (10%, but in some circumstances less) in an Australian agribusiness
- entering into certain agreements relating to the affairs of an entity or altering the constituent documents of an entity, which gives one or more foreign persons certain abilities to control senior officers of the entity, and
- entering into or terminating significant agreements with an Australian business.

Notifiable actions

The categories of notifiable actions extensively overlap with the concept of "significant actions". A foreign person who proposes to enter into an agreement to take a notifiable action must notify the Treasurer before entering into the agreement. Notifiable actions include:

- the acquisition of a direct interest (10%, but in some circumstances less) in an agribusiness
- the acquisition of a substantial interest (20% or more) in an Australian entity
- the acquisition of an interest in Australian land
- a foreign government investor starting a business in Australia or taking any direct interest (10%, but in some circumstances less) in an Australian entity or business, and
- a foreign government investor taking any interest in a tenement or a 10% or more interest in a mining, production or exploration entity.

Foreign investment requiring approval

The general rule is that investments of 20% or more by a single non-government foreign investor (and its associates) or 40% or more in aggregate by several foreign investors (and their associates) in an Australian business or corporation which is valued above (or the proposal values it above) a specified monetary threshold need approval.

The relevant monetary thresholds are set out below (current as at February 2019).

Monetary thresholds

The thresholds for foreign government and private investors are as follows (see table over page).

It should be noted that the higher thresholds applicable to certain free trade agreement partner countries (Chile, China, Japan, New Zealand, Singapore, South Korea and the United States) only apply in very limited circumstances where the foreign investor is investing directly from the relevant foreign country.

"Sensitive businesses" include media, telecommunications, transport, defence and military related industries and activities, encryption and securities technologies and communications systems, the extraction of uranium or plutonium or the operation of nuclear facilities.

Investment	Area/Type	Private investor nationality	Threshold (AUD)
Australian Business	Non-sensitive business	Chile, China, Japan, NZ, *Singapore, South Korea, US	$1,154 million
		All others	$266 million
	Sensitive business	All	$266 million
	Media	All	$0
Agriculture	Land	US, NZ, Chile	$1,154 million
		Thailand	$50 million
		All others	$15 million (cumulative)
	Agribusiness	US, NZ, Chile	$1,154 million
		All others	$58 million
Non-agriculture Land	Residential	All	$0
	Vacant commercial land	All	$
	Non-vacant commercial land	Chile, China, Japan, NZ, *Singapore, South Korea, US	$1,154 million
		All others	$266 million
	Lower threshold non-vacant land (eg,airport or port)	Chile, China, Japan, NZ, South Korea, US	$1,154 million
		All others	$58 million
	Mining and production tenements	US, NZ, Chile	$1,154 million
		All others	$0

**SAFTA now in force as of 1 December 2017*

Monetary screening thresholds are indexed annually on 1 January using the GDP implicit price deflator (except for the $15 million agricultural land threshold and the $50 million land threshold for investors from Thailand, which are not indexed).

Investment by foreign government investors

Any foreign government investor requires prior approval under the FATA irrespective of the investment amount if they are:

- starting a business in Australia;
- taking any direct interest (10%, but in some circumstances less) in an Australian entity or business;
- acquiring an interest in Australian land, or
- acquiring any interest in a mining, production or exploration tenement (irrespective of the duration of the tenement), or a 10% or more interest in a mining, production or exploration entity.

Foreign government investors may not have to seek prior approval when making passive investments of less than 10% in Australian entities or businesses.

Application fees

Each foreign investor applicant is required to pay a fee for each application made, or notice given, under the FATA. Very limited exceptions apply to application fees. The fee ranges from $2,000 to $103,400 per application.

Timing and process

On receipt of an application by statutory notice, the Federal Treasurer (acting on the recommendation of FIRB) has 30-40 days to decide whether to prohibit the proposed transaction on the basis that it would be contrary to the national interest.

FIRB has an additional 10 day period to advise the applicant of its decision. FIRB may also seek to extend the statutory period by a further 30 days.

In our experience, it is becoming more common that FIRB is requesting at least one extension before reaching a decision. Therefore applicants should be mindful of this and ensure that their FIRB applications are made as early as possible in the transaction process so as to avoid FIRB approval delaying completion of the transaction.

Approval by the Treasurer on advice from FIRB is normally only given for a specific transaction which is expected to be completed in a timely manner (usually 12 months).

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John has over 30 years' experience in mergers and acquisitions and has acted on some of Australia's largest and most complex corporate transactions. He has acted in both bid and defence roles in public listed company takeovers, majority shareholder sell-downs and mergers and spin-offs by scheme of arrangement.

John is numbered among "the top ten practitioners for public M&A in Australia" by a source quoted in Chambers Asia-Pacific 2016 and was named Best Lawyers® 2018 Sydney Commercial Law Lawyer of the Year.

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