Australian Shareholders' Association

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Director
Market Conduct Division
The Treasury
Langton Crescent
PARKES ACT 2600

Submitted by email: takeoversregulation@treasury.gov.au

AUSTRALIAN SHAREHOLDERS' ASSOCIATION – CORPORATE CONTROL TRANSACTIONS IN AUSTRALIA

Dear Ms McCallum

The Australian Shareholders' Association (ASA) represents its members to promote and safeguard their interests in the Australian equity capital markets. The ASA is an independent not-for-profit organisation funded by and operating in the interests of its members, primarily individual and retail investors, self-managed superannuation fund (SMSF) trustees and investors generally seeking ASA's representation and support. ASA also represents those investors and shareholders who are not members, but follow the ASA through various means, as our relevance extends to the broader investor community.

Thank you for the opportunity to comment on matters raised in the consultation paper, *Corporate control transactions in Australia: options to improve schemes of arrangement, takeover bids, and the role of the Takeovers Panel* (consultation paper).

We query the need for change, noting Gilbert + Tobin, Takeovers + Schemes Review 2022, states public mergers and acquisitions hit an all-time high, by volume and value, in 2021. The report also notes 79% of transactions were achieved by a scheme of arrangement, an increase from 50% in 2020.

ASA considers the current regime balances the need of companies for an efficient conduct of corporate actions with investor protections which are elevated due to the potential for shareholders assets to be compulsorily acquired against their wishes when 75% of the shares are voted in favour of a scheme.

Compulsory acquisition of exchange traded securities

As stated in the consultation paper, change of control transactions for exchange listed companies are typically enacted by two methods. The first is a takeover bid, governed by the Takeover Rules in Chapter 6 of the Corporations Act 2001 (the Corporations Act). In such a takeover, shareholders may choose to accept the offer, and compulsory acquisition is available to the bidder once 90% of shares under the offer have accepted. The second method is via a scheme of arrangement, a Court-approved regime governed by Chapter 5 of the Corporations Act (the Scheme of Arrangement Rules). Under such a scheme, if 75% of the votes (based on number of shares), and more than 50% of the shareholders voting on the resolution at the meeting (whether they are attending in person or by proxy) vote for the resolution, the shares of all holders will be acquired.

Compulsory acquisition transfers the ownership of the shares of holders who did not vote on a scheme or voted against the scheme resolutions, hence the importance of safeguards (particularly Court oversight, which we regard as a very important safeguard for retail shareholders), due process and protections.

Current regime provides investor protections

ASA considers ASIC and Court oversight, and the provision of independent expert reports, which provides additional scrutiny to be important protections for shareholders where their assets have the potential to be compulsorily acquired against their wishes.

Retail shareholders[1] have approached ASA on numerous occasions over many years, expressing their belief that takeovers (whether conducted as takeover bids or schemes of arrangement) are unfair to them. A summary of their concerns is they feel other shareholders, who have greater information and capacity to evaluate information, determine the outcome of a takeover, not retail shareholders.

We have counselled these shareholders to read all the documentation available to them and to make sure, in the case of schemes of arrangement, they have their say by voting on the scheme meeting resolutions. We advise them to take comfort in the process and not least the Court approval mechanism, notwithstanding the potential compulsory acquisition against their wishes.

Where the success rate of a scheme of arrangement of 89% in 2021 financial year (FY21) appears high, the level of success for deals initially launched without target board support for FY21 was 38%.[2] While greater success rate is attributed by some to shareholder trust in a target's board, it can signal to a minority shareholder whose shares have been acquired against their wishes, approval is automatic. We contend the process and obligations of the parties involved in the process contribute to the success rate.

[1] An individual non-professional investor who is not designated a wholesale investor or sophisticated investor
[2] Herbert Smith Freehills, Australian Public M&A Report 2021

Target board directors provide initial protection

On approach by a bidder, directors of the target company will not allow due diligence or put the offer to shareholders until a more reasonable price is reached.

Sydney Airport provides a recent example of the steps prior to putting a takeover via a scheme of arrangement to a vote of shareholders. On 5 July 2021[3], Sydney Airport announced to the exchange an unsolicited, indicative, conditional and non-binding proposal from a consortium of infrastructure investors to acquire, by way of scheme of arrangement and trust scheme, 100% of the stapled securities in Sydney Airport at an indicative price of A$8.25 cash per stapled security.

On 15 July 2021[4], the board announced to the exchange and shareholders that Sydney Airport will only progress a change in control transaction on terms that deliver and recognise appropriate long-term value for Sydney Airport Securityholders.

On 16 August 2021[5], the company advised a revised indicative proposal with a price of $8.45 was not considered to be in the best interests of shareholders. A revised proposal and intention to grant due diligence, at a price of $8.75 was announced 13 September 2021[6]

First Court hearing as a layer of protection

Once it is determined that a scheme is appropriate to be put before shareholders for voting, the first Court hearing examines the scheme details and documents. This is important as retail investors particularly rely on the proposers of the scheme being required to bring to the Court's attention all matters that could be relevant to the Court's exercise of its fairness discretion. Often, as a result of the Court scrutinising the scheme documents and matters brought to its attention by scheme proponents, the Court will require edits to be made to the scheme documents before it is prepared to make orders to convene the scheme meeting. This typically results in clearer disclosure of information, which is particularly beneficial for individual and retail investors.

Given many retail shareholders will not have a sophisticated understanding of the impact of the proposed transaction, the Court may order amendments to the scheme booklet. For example, in Re RGC Ltd (1998) 29 ACSR 445, the Court required a number of amendments to the scheme booklet so that (at 447) "the ordinary man, woman or company who sees the [scheme booklet] would be able to work out what the scheme is all about in such a way as to be able to exercise an informed vote."

Similarly, in Re Lifeplan Australia Friendly Society Ltd (No 1) [2009] VSC 640, Robson J stated (at [31]-[32]); "After reading the proposed explanatory statement, I have been left to speculate and infer on a number of points, when, in my opinion, the statement should be clear, forthright and unambiguous.

[3] Conditional, non-binding proposal for the acquisition of SYD
[4] Indicative Proposal not in best interests of Securityholders
[5] Revised Indicative Proposal
[6] Revised Proposal and intention to grant due diligence

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For these reasons, I am not fully satisfied that proper or clear disclosure has been made in the explanatory statement. Accordingly, I am not prepared to order a meeting to be summoned on the material presently before me, but I would be prepared to reconsider the matter if the following further evidence was provided."

For some other examples of the Court requiring changes to the scheme booklet, we highlight: Re Ardent Leisure Ltd [2018] NSWSC 1665 at [16][7] (amendments requested to clearly distinguish between the scheme proposal, a wider proposed restructuring that may be implemented after the scheme) and: Re NTM Gold Ltd [2021] WASC 22 at [46][8] (where ASIC's 14-day pre- review and Court's review of the contents of the draft scheme booklet led to amendments to ensure provision of full disclosure.)

Where an investor, such as UniSuper, a shareholder in Sydney Airport who exchanged its existing 15% interest in the Sydney Airport Securities for and interest in the acquiring consortium, experiences a different or additional benefit, a separate class of voting shareholder is created. The Court scrutiny of the draft document ensures this has occurred.

Independent expert report and documents are scrutinised by shareholders and media

While professional investors will be able to allocate time to assess the relevant information pertinent to voting on a scheme of arrangement during their business hours, retail investors may have difficulty fitting in a review of a complex proposal with all the other obligations that occupy their attention and time. For this reason, the approval of ASIC and the Court for distribution of the scheme booklet, is an added layer of surety.

Second Court hearing

With all of the examination that have preceded the second Court hearing, approval is not a foregone conclusion.

As example of Court dismissing a company's application for approval of a scheme took place in November 2016. It related to the proposed scheme of arrangement by which Asian Mineral Resources Limited (AMR) would acquire all of the issued capital of Kasbah Resources Limited (KAS) which was voted in favour by 92% of the shares. Subsequent to the vote, the Federal Court of Australia has dismissed the Company's application for approval of the scheme following objections raised by shareholders to the scheme. Considerations included the identification of a fundamental error in the Independent Expert's Report valuation methodology which led to a change to the opinion of the Scheme to "not fair, but reasonable" for Kasbah shareholders.

[7] http://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/nsw/NSWSC/2018/1665.html

[8] http://www.austlii.edu.au/cgi-bin/viewdoc/au/cases/wa/WASC/2021/22.html

We do not support the creation of a new procedure that does not have Court supervision

The ASA does *not* support the addition of a new procedure to Chapter 6 of the Corporations Act which would allow a target to convene a meeting and which would allow shareholders' shares to be compulsorily acquired following a 75% vote in favour.

The absence of the Court's supervision and scrutiny from such a procedure would be highly detrimental to retail shareholders. We do not believe that allowing any disputes to be heard by the Takeovers Panel to be an adequate replacement safeguard for retail shareholders. That would shift the cost and burden away from bidders and targets and onto retail shareholders. It is essentially saying that retail shareholders would need to protect themselves by closely scrutinising all the fine print in the complex transaction documentation and then incurring the cost of applying to the Takeovers Panel. We do not consider that to be fair or appropriate.

Court supervision of the entire scheme of arrangement process provides an important protection for retail shareholders and is one of the key reasons why a 75% vote is an acceptable threshold for compulsory acquisition in a scheme whereas the threshold is 90% in a takeover.

If, despite our view, the Government introduced an additional procedure, we consider that the voting approval threshold should be set at 90% not 75% to compensate for the absence of Court protection. And, even in that scenario, we would want to see the existing scheme of arrangement procedure (with Court approval) retained in Chapter 5 of the Corporations Act. In other words, there would then be two procedures.

Takeovers panel can't replace court and would need to build "small investor" expertise

The Takeovers Panel is comprised of part-time members. If, despite our strong views above, the obligation for schemes of arrangement transferred to the Panel, the members would need to build expertise in the protection of small shareholders.

We also note that where a takeover using scrip is achieved by a scheme of arrangement, foreign prospectus exemptions are only available if the transaction is approved by a Court. Trust schemes (as are common in the Real Estate and Infrastructure sector) also require judicial advice from a Court.

In researching content for this paper, ASA noted alternative proposals to improve efficiencies in takeovers without reducing the protections in place for smaller shareholders in Allens' *Insights* article dated 5 April 2022, authored by Guy Alexander and Charles Ashton, *Should the Takeovers Panel have jurisdiction over schemes?*[9] Suggestions which should be investigated include the introduction of a mandatory bid rule, which would allow acquisitions above the 20% takeover threshold if it was immediately followed by a bid for all of the remaining shares on the same terms and conditions and the introduction of a

[9] https://www.allens.com.au/insights-news/insights/2022/04/Should-the-Takeovers-Panel-have-jurisdiction-over-schemes

mandatory non-waivable 50.1% minimum acceptance condition, to prevent an existing major shareholder using a nil or low premium offer to increase control below 50%.

In summary, ASA considers the current regime balances the need of companies for an efficient conduct of corporate actions with investor protections.

If you have any questions about these comments or other matters, please do not hesitate to contact me, or Fiona Balzer, Policy & Advocacy Manager on (02) 9252 4244.

Yours sincerely

Rachel Waterhouse
Chief Executive Officer
Australian Shareholders' Association