

# The Market For Corporate Control: Promoting Productive Investment

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*This article describes the Government's proposed reforms to the takeover provisions of the Corporations Law that are intended to complement and enhance the improvements to the operation of financial markets arising from the Wallis reform process.*

## INTRODUCTION

Takeovers, or the prospect of takeovers, provide benefits for shareholders, the corporate sector and the wider economy. In particular, they provide incentives for improved corporate efficiency and enhanced management discipline, leading ultimately to greater wealth creation.

The Corporate Law Economic Reform Bill, introduced into the Parliament by the Treasurer on 2 July 1998, contains proposed new regulatory arrangements that will remove unnecessary obstacles to takeovers by:

- promoting a more competitive market for corporate control;
- improving the resolution of takeover disputes;
- extending the takeover provisions to listed managed investment schemes;
- streamlining the rules for both off-market and market bids; and
- rationalising the liability provisions.

## A MORE COMPETITIVE MARKET

The key reform to the Corporations Law that has attracted most attention is the introduction of the 'mandatory bid rule'. This will allow a bidder to exceed the statutory threshold of 20 per cent of total voting rights to gain control of a target, provided that the announcement of a full, unconditional takeover bid immediately follows the acquisition that takes the bidder through the threshold.

The mandatory bid rule is based upon a similar one used in the United Kingdom, and provides two significant advantages over the current takeover regime. First, by giving potential bidders the choice of which takeover method to employ, they are more likely to proceed with their bids. Under the current system, bidders incur costs in identifying and analysing target companies. If rival bidders force an auction for control, they can 'free-ride' on the information

produced by the initial bidder. Hence, there is less incentive for bidders to engage in searching for potential targets. The mandatory bid rule will reward bidders willing to put up search costs by giving them the opportunity to secure control without an auction. More investment in research can be expected to result in more takeover bids.

The second advantage is that the rule will ensure that all target company shareholders will have the opportunity to sell their interest at a fair price and to benefit from the premium a bidder for control places on the securities.

Subject to some minor modifications to provide protections for minority shareholders, the general procedure for undertaking a mandatory bid will be the same as for other takeover bids. These modifications include that the bid must be unconditional, target shareholders must be provided with an independent expert's report by the target, the bidder must not exercise control of the target until the mandatory bid is made, and no securities may be issued in the target company from the time of the pre-bid acquisition until the end of the bid period without shareholder approval by a general meeting.

A further limitation is that the mandatory bid rule may only be used in situations where the bidder starts from below the 20 per cent threshold, with only one acquisition being allowed before the mandatory bid requirement is triggered. The Government will review the operation of the rule two years after its commencement to ensure that its objectives are being achieved.

The compulsory acquisition rules will be broadened in recognition of the benefits accruing to majority shareholders from achieving 100 per cent ownership. These benefits include the better management of company groups and reduced transaction costs related to the administrative and reporting requirements of associated companies.

The rules will allow all types of securities (not just shares) to be compulsorily acquired, and for compulsory acquisitions to take place at any time, not just following a takeover bid. The rules will facilitate the acquisition of the outstanding securities in a class by any person who already holds 90 per cent of the class. They will also provide for the acquisition of all the securities, in all classes, of a target, where overwhelming ownership of the target by the majority shareholder can be demonstrated.

## **BETTER DISPUTE RESOLUTION**

Under the current takeover provisions, bids for corporate control can be disrupted as a result of litigation. It is argued that target companies may sometimes resort to litigation for tactical reasons. Where a final hearing cannot be held within the bid period, the courts have to decide between disrupting the bid by granting an injunction without the benefit of full evidence and allowing the bid to proceed even though it may later be found to be defective. In both

instances, considerable extra costs can be imposed on the bid process. The threat of costly litigation may act as a deterrent to the initiation of takeover bids, even where the benefits of proceeding with a takeover bid are clear.

Reforms will be put in place to expand the role of the Corporations and Securities Panel (the Panel) so that it, rather than the courts or the Administrative Appeals Tribunal (AAT), becomes the primary forum for resolving takeover matters. This will be achieved by opening up access to the Panel to any interested party (rather than being limited to the Australian Securities and Investments Commission (ASIC) as at present), reducing the scope for court proceedings in relation to a takeover bid during the bid period, and having the Panel, rather than the AAT, review ASIC exemption and modification decisions relating to takeovers.

As a result of these reforms, takeover disputes will be resolved as quickly and efficiently as possible by a specialist body largely comprised of takeover experts, so that the outcome of the bid can be resolved by the target shareholders on the basis of its commercial merits, and court resources will be freed to attend to other priorities.

## **TAKEOVERS OF LISTED MANAGED INVESTMENT SCHEMES**

By applying the takeover provisions to listed managed investment schemes, members of these schemes will have the same rights to share in a control premium as shareholders, while responsible entities of these schemes will face the same competitive pressure to perform as company directors.

In order to apply the company takeover provisions to listed managed investment schemes, the provisions equate features of a company to features of a managed investment scheme where practical. However, in some instances, the application of the provisions to listed managed investment schemes is specifically dealt with. In addition, the regulations may modify the application of the takeover provisions to listed managed investment schemes.

## **STREAMLINING TAKEOVER PROCEDURES**

Reforms to the procedures that must be followed by bidders and target companies will clarify the current rules, and remove anomalies and unnecessary requirements in order to reduce transaction costs and lighten the regulatory burden on business.

The reforms include bringing together disclosure requirements into a bidder's statement (replacing the current Part A and Part C statements) and a target's statement (replacing the current Part B and Part D statements). These statements will facilitate better disclosure by replacing the checklist of content rules with a

general disclosure requirement for all information of relevance to a shareholder's decision whether or not to accept an offer.

Other reforms include measuring voting control of a company by the number of votes attached to shares a person controls, rather than the number of voting shares (more accurately reflecting a person's voting power), and liberalising the current exemption for downstream acquisitions that occur as a result of an acquisition of shares in an Australian listed company (the upstream acquisition). This is achieved by allowing the upstream acquisition to fall under any of the exemptions from the 20 per cent threshold and extending the exemption to foreign bodies approved by ASIC.

## **LIABILITY PROVISIONS**

The reforms will ensure that the liability regime for the content of takeover disclosure documents is generally consistent with that applying to the proposed new fundraising rules.

A person must not give a takeover or compulsory acquisition document that contains a misleading or deceptive statement, omits material or fails to disclose a new circumstance. Consistent with the approach taken in the proposed fundraising provisions, liability for a defective takeover or compulsory acquisition document will be dealt with under a specific liability regime to the exclusion of the general prohibition on misleading or deceptive conduct. This will make it clear that the positive disclosure obligations in relation to these statements are reinforced by a specific liability and defence regime. The misleading and deceptive conduct provisions in the Trade Practices Act (and the equivalent provisions in the State and Territory Fair Trading Acts) will no longer apply to securities dealings.

## **CONCLUSION**

The proposed reforms to the takeover provisions will enhance competition in the market for corporate control. They complement the other components of the Corporate Law Economic Reform Program in modernising the Corporations Law and giving it an economic focus by introducing world best practice in business regulation. By streamlining business practices and reducing red tape, Australian businesses will be better placed to grow and create jobs.