Developments in Contested Bids

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SUMMARY

This paper looks at three important issues which affect contested takeover bids. First, it reviews the recent case law concerning the form of disclosure of the offeror's intentions that is required in Pt A Statements. It is argued that the use of vague and general formulations needs to be approached with care. Regard should be had to the offeror's pre-bid analysis, relevant management and board submissions, material supplied by the offeror to other parties and any prior communications between the offeror and the target.

Secondly, the paper considers whether Pt A Statements relating to scrip bids should include earnings forecasts. Earnings forecasts may be "material" to the decision of an offeree on whether to accept a takeover offer within the meaning of cl 17 of Pt A of s 750 of the Corporations Law. Because of this, it is argued that Pt A Statements in respect of scrip bids should include earnings forecasts.

Thirdly, this paper considers some of the interesting attempts at preventing offerors from utilising the compulsory acquisition provisions of Ch 6 of the Corporations Law. In particular, it reviews recent cases concerning "share-splitting" arrangements. It is argued that it is correct to prohibit such blatantly artificial devices.

INTRODUCTION

It is a feature of the commercial landscape in this country that unwelcome takeover bids will frequently give rise to litigation. In many cases the litigation will involve the target company or a competing bidder alleging that the offeror's takeover documentation is deficient in the disclosures made, particularly in the area of the offeror's intentions.

In the past few years there has been a number of takeovers involving resource companies which have given rise to litigation. The decisions in these cases are not always easy to reconcile but are very important for anyone advising in relation to a takeover, in particular those advising in relation to the preparation of the bid documents.

The object of this paper is to examine the impact of these recent cases on the form of disclosure in Pt A Statements of the offeror's intentions and whether it is necessary for Pt A Statements to include earnings forecasts as part of the required disclosure.

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The paper will also examine the recent "share-splitting" arrangements undertaken by Mr John Thompson in a number of takeovers and look at their impact on the application of the compulsory acquisition provisions of Ch 6 of the *Corporations Law* (the Law).

DISCLOSURE OF THE OFFEROR'S INTENTIONS

The disclosure of the offeror's intentions in takeover documentation has always been a difficult issue and has provided a fertile basis for takeover litigation.[1]

A valid Pt A Statement must comply with the requirements of Pt A of s 750 of the Law (s 603). The disclosure of certain intentions on the part of the offeror is required by cl 20 of Pt A of s 750, which is in the following terms:

> "20(1) The statement shall set out *particulars of* the offeror's intentions regarding:
> (a) the continuation of the business of the target company;
> *(b) any major changes to be made to the business of the target company, including any redeployment of the fixed assets of the target company; and*
> (c) the future employment of the present employees of the target company.
>
> 20(2) Without limiting the generality of subclause (1), if the offeror has not made a decision on a matter referred to in paragraph (1)(a), (b) or (c) but is considering a possible course of action, or two or more possible courses of action, in relation to that matter, the statement shall set out that fact and *specify* the course of action or courses of action concerned and the reason why the offeror has not made a decision on the matter" (emphasis added).

There is a similar requirement set out in cl 15 of Pt C of s 750 and the discussion that follows in relation to Pt A Statements is just as relevant to the disclosure of the offeror's intentions in a Pt C Statement.

The commercial difficulty that cl 20 poses for offerors is that detailed descriptions in Pt A Statements of radical changes an offeror intends to make to the business of the target company, whether by way of the disposal of substantial assets or the termination of the employment of a significant number of the target company's employees, will generally have the effect of stiffening the resistance of the target and therefore detracting from an offeror's prospects of a successful bid. The natural tendency is therefore for offerors and their advisers to seek to draft the information relating to the offeror's intentions in vague and general terms. In support of this position

[1] *Peters (WA) Ltd v National Companies and Securities Commission* (1986) 13 ACLR 487; *Australian Consolidated Investments Ltd v Rossington Holdings Ltd* (1992) 10 ACLC 600; *Cumberland Credit Corp Ltd v TNT Aust Pty Ltd* (1988) 13 ACLR 371; *ICAL v County Natwest Securities Aust Ltd* (1988) 13 ACLR 129; *Samic Ltd v Metals Exploration Ltd* (1993) 60 SASR 300.

one can argue that the offeror will often have limited knowledge about the business, assets and employees of the target and is therefore not in a good position to form specific intentions which can be particularised in the Pt A Statement.

Not surprisingly in practice it has been common in Pt A Statements to find the intentions of offerors stated in a very general way. The following have been commonly occurring features of such general intention statements:

1. The offeror intends to carry out a study of the business of the target and confer with management of the target to work out which operations and assets of the target are surplus to the ongoing requirements of the merged enterprise post-takeover.
2. Following completion of such study and discussions any operations or assets identified as surplus will be disposed of on the best terms commercially available having regard to the then prevailing market conditions.
3. The head office functions of the target company will be merged with the head office of the offeror with some resulting loss of employment which the offeror will endeavour to minimise.
4. Subject to the above, the offeror intends to continue the business of the target, not to make any major changes to the business or to redeploy any fixed assets and to continue the employment of the target company's employees.

The difficulty for anybody involved in the preparation of bid documentation lies in being satisfied that the intentions statement satisfies the requirements of cl 20. The commercial background against which such statements of intention are prepared is that the offeror will have undertaken a detailed financial analysis of the proposed takeover to determine projected post-takeover earnings and cash flow of the merged entity prior to deciding to proceed with the takeover bid. This financial analysis will invariably factor in various assumptions as to asset disposals and operating cost reductions resulting from, amongst other things, workforce rationalisation. To undertake a takeover without undertaking such analysis would raise issues as to whether officers of the offeror had exercised a suitable degree of care and diligence in carrying out their duties. There will usually be a range of differing assumptions factored into this financial analysis. While it is trite that these assumptions do not necessarily constitute intentions on the part of the offeror, it needs to be kept in mind that they may constitute evidence of possible courses of action under consideration by the offeror. The substance of this pre-takeover analysis may accordingly be relevant in the context of the disclosure required by cl 20(2).

The Practice Note[2] issued by the Australian Securities Commission (ASC) in relation to the requirements of cl 20 is of little assistance in practice and is in need of revision following the decisions referred to below.

[2] Practice Note 35, issued 19 July 1993.

The disclosure requirements of cl 20 were central issues in *Gantry Acquisition Corp v Parker & Parsley Petroleum Australia Pty Ltd*[3] and *Ampolex Ltd v Mobil Exploration & Producing Australia Pty Ltd*.[4]

In the *Gantry* case, Parker & Parsley Petroleum Australia Pty Ltd (Parker & Parsley) had made offers for all the shares in Bridge Oil Ltd (Bridge), as had Gantry Acquisition Corp (Gantry). Parker & Parsley sought and obtained an injunction in the Federal Court restraining Gantry from despatching its offers to Bridge shareholders on the grounds that Gantry's Pt A Statement did not comply with the disclosure requirements of cl 20 of Pt A of s 750. Gantry appealed that decision to the Full Federal Court.

Gantry's intention statement was set out in the Pt A Statement in two clauses, which read as follows:

> "15.1 Gantry intends to proceed to compulsory acquisition of all outstanding Bridge Oil shares immediately upon it becoming entitled to do so as a consequence of acceptances of the offers. Gantry intends ultimately to concentrate its activities to within the USA. Consequently, Gantry intends to cause Bridge Oil to divest its non-US operations and assets at an appropriate time and on the most favourable terms. Options under consideration are sales of assets in whole or in part, and a possible Australian, public offering of all or a portion of the non-US operations and assets. Gantry has not made a decision in respect of those options because it is not yet in possession of sufficient information necessary to make such a decision. Any decisions in relation to the non-US operations and assets would be determined after Gantry has examined those operations and assets and further considered its position and will be evaluated in light of prevailing market conditions. Gantry intends that the non-US operations and assets would continue to be managed in the best long-term interests of those operations and assets. Gantry intends to cause BOUSA [a US subsidiary of Bridge] to sell to Cactus Hydrocarbons III, a limited partnership in which Enron Cactus III Corp is the general partner, a term overriding royalty interest (a real property interest in leases, entitling the holder to ownership of the oil and gas in the ground) in its South Texas oil and gas leases for a purchase price of approximately US$60M.
>
> 15.2 Subject to paragraph 15.1, Gantry:
>
> (a) intends to continue the business of Bridge Oil and its subsidiaries;
>
> (b) does not intend to make any major changes to the business of Bridge Oil and its subsidiaries or to redeploy the fixed assets of Bridge Oil and its subsidiaries; and
>
> (c) intends to continue the future employment of the present employees of Bridge Oil and its subsidiaries."

[3] (1994) 14 ACSR 11.

[4] (1996) 19 ACSR 354.

It is obvious at once that the statements are fairly general in nature and not dissimilar to the general form of intentions statement commented on earlier. The disclosure required by cl 20(1) is made on an exception basis (that is, "except as may be contrary to the general intentions set out above Gantry intends to ...") but as noted this was not unusual.

The majority (Sheppard and Burchett JJ) held that the Pt A Statement was seriously flawed because of non-compliance with cl 20. The reasons are interesting and illustrate the difficulties facing those preparing such statements.

Sheppard J acknowledged the tension that exists between the disclosure required by cl 20 and the commercial background against which the offeror's intentions are formed:

> "I have taken into account the fact that it is particulars which cl 20 requires. I bear in mind also that cl 20(2) uses the word 'specify'. Accordingly, an offeror must do the best it can to be particular and specific about its intentions. Nevertheless the document is dealing with a commercial situation. It is being delivered in a context in which the offeror does not have control of the target company. In those circumstances it is not only reasonable, it is also necessary, for it to express itself in a guarded way. If it does not do this, it runs the risk that statements it makes may, because of their very particularity, be found to have been misleading."[5]

The Pt A Statement contained no indication in cl 15 (or elsewhere) as to what Gantry intended to do with the US$60 million it expected to obtain from the selling of the term overriding royalty interest. Sheppard J thought that this was a fatal omission.

> "In my opinion, a reader of the Pt A Statement is not being informed sufficiently of the appellant's intentions. The absence of information, which I think I should infer must exist, may put a shareholder contemplating acceptance of the offer at a significant disadvantage because he is not told of the precise nature of what is intended and, importantly, of what is to happen to the US$60 million. It is true that, upon the hypothesis that the appellant will acquire the whole of the shares in Bridge Oil, the acceptor is unlikely to be interested in any financial or commercial way in the outcome of the projected sale, but further particularisation and an indication of the ultimate destination or use of the money would give him an idea of how important the acquisition was to the appellant. It would better enable him to gauge the likelihood or otherwise of his being able to gain an increased offer by refusing acceptance for the time being. It is a question of being given full and sufficient information to make a judgment concerning how valuable the acquisition will be to the appellant and thus of making an informed assessment of whether the appellant may be prepared to pay more for the shares than its offer suggests."[6]

[5] (1994) 14 ACSR 11 at 17.
[6] Ibid at 18-19.

His Honour also held that the failure to include information on how the sale price was intended to be utilised breached cl 17 of Pt A of s 750, which requires the disclosure of material information known to the offeror. Of note is the willingness to infer that the relevant information did exist.

In the course of his judgment, Burchett J considered the nature of the disclosure required by cl 20 and observed:

> "These [cll 17 and 20] are important provisions, plainly reflecting a legislative determination to ensure that a detailed disclosure is made in a Pt A Statement of all matters material to a shareholder's decision whether or not to accept the offer made. There are a number of indications of the comprehensiveness of the disclosure required. It is clear that it embraces both information bearing on the bargaining possibilities of the situation, including the value to the offeror of the interest sought to be acquired, and also information bearing on a concern, perhaps unrelated to economics, which some shareholders may have for the future of the enterprise itself, or of its employees. But the extent of the area of disclosure is matched, as an indication of the seriousness of the legislative requirements, by the precision of the detail also demanded. Clause 20(1) requires 'particulars', not an outline or a general statement; while 20(2) precludes an offeror from simply saying no decision has been made, where he is considering a possible course of action or possible courses of action — in such a case 'the statement shall set out that fact and *specify* the course of action or courses of action concerned and the reason why the offeror has not made a decision on the matter'. I have emphasised the word specify because it is a word which leaves no doubt that precision is essential. It should be noticed too that clause 20(2) carefully preserves the full meaning of clause 20(1) by the opening words: 'Without limiting the generality ...'."[7]

Having made those observations Burchett J went on to find that the Pt A Statement did not comply with the requirements of cl 20 for a number of reasons including inconsistency between the substance of paras 15.1 and 15.2, the failure of the offeror to specify what it intended to do with the proceeds of sale of the term overriding royalty interest and that the form of cl 15 was misleading. Of particular interest are his Honour's comments on the relationship between paras 15.1 and 15.2, which he thought made the Pt A Statement misleading.

> "In the first place, the statement of an intention to dispose of the Australian operations is so muffled in subpara (1) by expressions such as 'ultimately', 'at an appropriate time', 'after Gantry has .... further considered its position' and 'Gantry intends that the non-US operations and assets would continue ...', that the precise statements in subpara (2) stand out like beacons against a cloudy background, and the fact that they are said to be 'subject to' so much vagueness

[7] Ibid at 23.

> would be unlikely to be noticed by many readers. That is calculated to deceive. It is especially calculated to deceive those readers who want to hear the very points that are so clearly and succinctly stated against the letters (a), (b) and (c) of subpara (2). Accordingly, I think that the *form* of paragraph 15 is calculated to deceive" (emphasis added).[8]

Beazley J, in a dissenting judgment, did not think that the form of the intentions statement rendered the Pt A Statement invalid. While the reasoning of the majority is not the same there is in the writer's opinion no reason why it would not be followed.

The *Ampolex* case arose out of a takeover bid by Mobil Exploration & Producing Pty Ltd (MEPA) for shares in Ampolex Ltd (Ampolex). It received a lot of publicity at the time because, amongst other things, Ampolex was then embroiled in litigation with a convertible noteholder over the rate at which the notes converted into shares. The *Ampolex* case involved proceedings by Ampolex to restrain the dispatch of offers by MEPA, based on its Pt A Statement, which was alleged to be deficient in a number of respects. One of these was that the intentions statement did not comply with the requirements of cl 20 of Pt A of s 750.

In the original Pt A Statement MEPA's statement of intentions was in the following form:

> "18 On the basis of the information concerning Ampolex known to MEPA at the date of this Statement, and subject to the matters referred to in this section, it is the intention of MEPA, if the Takeover Scheme is successful, that:
>
> (a) the business of Ampolex be continued in the same manner as it is presently being conducted;
>
> (b) no changes be made in the business of Ampolex and there not be any re-deployment of the fixed assets of Ampolex; and
>
> *(c) the employment of the present employees of Ampolex be continued.*
>
> If the Takeover Scheme is successful, MEPA proposes to discuss with the senior executives and management of Ampolex the best way to utilise the assets and the experience and expertise of employees of Ampolex for the benefit of MEPA and other members of the Mobil Group.
>
> In accordance with usual practices engaged in by MEPA and other exploration and producing (E&P) affiliates of the Mobil Group, as well as other corporations involved in the oil and gas exploration and production industry (including Ampolex), all of Ampolex's assets will be subjected to regular scrutiny and review as to performance and prospectivity.
>
> In relation to Ampolex's assets in the United States of America, MEPA notes the comments made in the Ampolex *1995 Annual Report* that:
>
> 'The financial contribution of the Company's United States assets is under close scrutiny, with a commitment to improve the value-generation potential and return on funds invested.

[8] Ibid at 26.

Associated with this commitment, a review of existing United States assets has been completed with the steps taken to orientate future activities to achieve maximum value generation and to continue the process, already well advanced, of disposing of lower-contributing and non-core assets. In line with the Company's overall commitment to deploy resources to areas of greatest potential value, the performance of United States assets will be an important determinant of the nature and extent of Ampolex's continued operations in the country.'

MEPA proposes to discuss the review process identified by Ampolex with senior executives and management of Ampolex to determine whether the United States assets should be retained, merged with existing assets of other Mobil E&P affiliates or divested.

MEPA recognises that an issue which will need to be resolved is the rationalisation of functions presently carried on by the respective Australian offices of both Ampolex and MEPA. MEPA intends to identify and realise potential cost savings associated with avoiding duplication of functions."

Again, the statement is very general in its form. Ampolex alleged it was defective and in breach of cl 20 because it did not disclose that MEPA had in place a well developed strategy to inject massive financial and management resources into Ampolex.

The evidence was that on the date it announced its intentions to bid for Ampolex the Mobil group had written to Ampolex. The following passages are taken from the relevant letter:

"Mobil's interest in Ampolex reflects the complementary fit between our two companies. To participate fully and successfully in the development of its resource base, Ampolex will require not only massive financial and management resources, but also world class skills and strengths in development, technology, project management, project finance, production, operations, marketing and logistics. Mobil can supply all of these. By integrating into a major international oil company, Ampolex will be able to successfully accomplish the challenging next phase of your announced asset development program ...

Mobil's strategy to maintain and build on Ampolex's existing operations in the Australian and Papua New Guinea region is unique, because Mobil has a high interest in pursuing an active future in the Australian area but we currently have only a very small staff. Our intent is to work with you and your people to build for the future on the bases that Ampolex has created."

Sackville J of the Federal Court made certain findings as to the facts and then found s 18 of the Pt A Statement was defective because it did not satisfy the requirements of cl 17 of Pt A of s 750 and was misleading and deceptive. His Honour did not make a final finding as to whether the requirements of cl 20 had been adequately complied with but observed:

"The point is not that MEPA is obliged to specify in a Pt A Statement the details of all plans it is considering for Ampolex's future operations. In order to avoid misleading shareholders it is clearly necessary for an offeror to couch its language carefully. It is also necessary to avoid speculation. General statements may well be enough, especially if intentions cannot be formulated precisely until after a takeover is completed. For example, I am not satisfied that the reference in s 18 of the Pt A Statement to the possible divesting of Ampolex's assets, despite its generality, can be regarded as a breach of cl 20, or as misleading or deceptive within s 995(2) of the Law. But the defect in s 18, in my opinion, is not merely that it omits material information. It is that it creates the impression that MEPA is much less advanced in its planning with respect to the development and exploitation of Ampolex's underperforming resource base than is in fact the case.

It is material to a shareholder's decision whether or not to accept a takeover offer that the offeror, after careful consideration over several months, intends to integrate the business into the offeror's world wide operations; to provide the financial and management resources to exploit the target company's underperforming resource base (including providing the finance of at least $1.7 billion for particular projects); and to consider a strategy to create a market for gas produced from an important field within that resource base. It is, in my opinion, likely that many Ampolex shareholders would be misled by the bland statements to which I have referred, since they would not be alerted to the reasons for MEPA making the takeover offer, nor to the overall strategy and indeed specific proposals MEPA plainly had in mind to improve Ampolex's performance and to ensure that its resource base is fully exploited."[9]

It seems likely to the writer that the requirements of cl 20 will continue to provide fertile ground for litigation. In part this may be attributable to the fact that the circumstances of each takeover will differ and accordingly there is no general formulation that can be relied on to satisfy those requirements.

The courts are requiring offerors to be particular and specific as to these intentions while acknowledging that these intentions might be expressed in a guarded way in order to avoid misleading offerors. The use of vague and general formulations needs to be approached with care. Careful regard should be had to the offeror's pre-bid analysis, relevant management and board submissions, material supplied by the offeror to other parties (for example, the Foreign Investment Review Board (FIRB), the Australian Competition and Consumer Commission (ACCC) or bid financiers) and to any prior communications between the offeror and the target when considering the form of the intentions statement. Because the courts have

[9] (1996) 19 ACSR 354 at 384.

found[10] that a proper statement of the offeror's intentions goes to the fundamental matter of an offeree's assessment of the prospects of receiving a higher offer it can be expected that intentions statements will continue to be subjected to exacting scrutiny.

DISCLOSURE OF EARNINGS FORECASTS

As noted previously, a valid Pt A Statement must comply with the requirements of Pt A of s 750. In order to determine whether an earnings forecast should be included in bid documentation it is necessary to consider the requirements of cll 17 and 18, which read as follows:

> "Other material information
>
> 17 The statement shall set out any other information material to the making of a decision by an offeree whether or not to accept an offer, being information that is known to the offeror and has not previously been disclosed to the holders of shares in the target company.
>
> Information required by regulations to be disclosed
>
> 18 If the statement:
>
> (a) is included in a class of Part A statements in relation to which regulations are in force for the purposes of this paragraph;
>
> (b) relates to an offer to acquire shares in a class of offers in relation to which regulations are in force for the purposes of this paragraph; or
>
> (c) relates to an offer to acquire shares where the consideration specified in the offer as the consideration for the acquisition of shares is or includes marketable securities in a class of marketable securities, or is or includes marketable securities of a body corporate in a class of bodies corporate, in relation to which regulations are in force for the purposes of this paragraph;
>
> the statement shall set out the *prescribed* matters and contain the prescribed reports, being reports each of which either indicates by way of note any adjustments as respects the figures of any profit or loss or assets and liabilities dealt with by the report that appear necessary to the person making the report or makes those adjustments and indicates that adjustments have been made" (emphasis added).

Regulation 6.12.02(2) and (3) sets out the prescribed information for the purposes of cl 18 in respect of scrip bids. If the securities being offered as part of the offer consideration are quoted ED securities and certain other requirements are satisfied then the Pt A Statement must include the information which would be included in a prospectus under of s 1022AA. If the securities offered as part of the offer consideration are not quoted ED securities then the Pt A Statement must include the information which would be included in a prospectus under of s 1022 of the Law.

[10] *Samic Ltd v Metals Exploration Ltd* (1993) 60 SASR 300; *Gantry Acquisition Corp v Parker & Parsley Petroleum Australia Pty Ltd* (1994) 14 ACSR 11.

In order to understand the disclosure requirements of cl 18 it is necessary to examine briefly the legal requirements applying to prospectuses. The advent of the Law brought with it significant changes to the capital-raising regime in this country. Amongst the most significant of these changes was the move away from specific prescriptive requirements in relation to the content of prospectuses and the introduction of a more general requirement embodied in s 1022.

Section 1022(1) of the Law provides as follows:

> "1022(1) [Information to be included] In addition to the information required by section 1021 to be included in a prospectus in relation to securities of a corporation other than a prospectus to which section 1022AA applies, such a prospectus shall, subject to subsection (2), contain all such information as investors and their professional advisers would reasonably require, and reasonably expect to find in the prospectus, for the purpose of making an informed assessment of:
> (a) the assets and liabilities, financial position, profits and losses, and prospects of the corporation; and
> (b) the rights attaching to the securities."

An early problem for those advising on capital raisings under the new regime was whether investors and their professional advisers would reasonably require and reasonably expect to find a forecast of future earnings of the issuing corporation in a prospectus in order to make an informed assessment of the prospects of that corporation or, put another way, whether there was a legal requirement to include such a forecast. The introduction of the Law saw the advent of s 765. Section 765 was a new provision (although it had been in the *Trade Practices Act* 1974 (Cth) for some time) which effectively deemed representations as to future matters, including earning forecasts, to be misleading *unless* the person making the representation could prove to the contrary. This reversal of the onus of proof and the new liability regime resulted in some nervousness about the inclusion of earnings forecasts in prospectuses.

Whatever the early history, the legal position appears to be that for those corporations issuing a prospectus under s 1022 the information "investors and their professional advisers would reasonably require and reasonably expect to find in a prospectus" should be determined having regard to prevailing market practice and the nature of the offer being made by the issuing corporation.

It should be noted that market practice may change from time to time with a consequent change in the information required under s 1022 to be included in a prospectus. One factor in this evolution in the market practice will be the requirements of underwriters of issues as to the content of prospectus documents which will be used to sell securities into an increasingly competitive global market.

Some broad generalisations may be made of the market practice as it developed in Australia prior to the enactment of s 1022AA in 1994. First, it was common for companies undertaking initial public offerings to include quantitative profit forecasts in the prospectus. The period in respect of

which such forecasts are given is variable but it is not unusual to go out two years or more from the date of issue of the prospectus. Secondly, it was not uncommon for issuers undertaking rights issues to existing shareholders to raise funds for debt retirement and working capital (as against the funding of specific acquisitions) not to include quantitative profit forecasts and for the prospects of the corporation to be addressed generally in narrative form.

The introduction of s 1022A was intended to simplify the content of prospectuses issued by a disclosing entity in relation to ED securities. "ED securities" are defined in s 111AD of the Law. They include, but are not limited to, securities in a class of securities that are quoted on a stock market of a securities exchange; that is, shares quoted on the Australian Stock Exchange (ASX) are ED securities. Corporations that issue ED securities are "disclosing entities" pursuant to s 111AC. Disclosing entities must comply with the disclosure requirements of ss 1001A or 1001B depending upon whether or not they are listed disclosing entities.

Section 1001A, which applies to listed disclosing entities, obliges such entities to comply with the disclosure requirements of the Listing Rules of the stock exchange on which they are listed. The principal disclosure requirement in the ASX Listing Rules is Listing Rule 3.1:

> "3.1 Once an entity is or becomes aware of any information concerning it that a reasonable person would expect to have a material effect on the price or value of the entity's securities, the entity must immediately tell ASX that information. This rule does not apply to particular information while each of the following applies:
>
> 3.1.1 A reasonable person would not expect the information to be disclosed.
>
> 3.1.2 The information is confidential.
>
> 3.1.3 One or more of the following applies:
>
> (a) It would be a breach of a law to disclose the information.
>
> (b) The information concerns an incomplete proposal or negotiation.
>
> (c) The information comprises matters of supposition or is insufficiently definite to warrant disclosure.
>
> (d) The information is generated for the internal management purposes of the entity.
>
> (e) The information is a trade secret."

The point to note is that, under the Listing Rule, there are exemptions or carve-outs from the requirement to disclose all price sensitive information that is not generally available.

The underlying rationale for the amendments introduced by s 1022AA is that, subject to an important qualification, corporations that are disclosing entities will by virtue of the continuous disclosure regime have disclosed to the market all information that is not generally available and that a reasonable person would expect, if it were generally available, to have a

material effect on the price or value of ED securities of the entity. On that basis there is accordingly no need for offerees of ED securities to be provided with the extensive information required by s 1022.[11]

The principal content requirement under the s 1022AA regime is found in subs (2):

> "1022AA(2) [Requirements for prospectus] In addition to the information required by section 1021 to be included in the prospectus, the prospectus must:
> (a) set out the terms and conditions of the offer or invitation contained in the prospectus; and
> (b) contain all such information as investors and their professional advisers would reasonably require, and reasonably expect to find in the prospectus, for the purpose of making an informed assessment of:
> (i) the effect of the offer or invitation on the disclosing entity; and
> (ii) the rights attaching to the securities; and
> (c) contain a statement that:
> (i) explains that the disclosing entity, as such an entity, is subject to regular reporting and disclosure obligations; and
> (ii) advises that copies of documents lodged in relation to the entity may be obtained from, or inspected at, an office of the Commission."

It can be seen at once that there is nothing in this formulation that specifically requires inclusion in a prospectus, to which s 1022AA applies, of information in relation to the future prospects of the issuing corporation. This is because all such information will presumably be in the marketplace (having been disclosed under the continuous disclosure regime) and offerees wishing to access such information can do so through the ASC.

However, as has been noted, Listing Rule 3.1 does not require the disclosure of all price sensitive information that is not generally available. In particular it would seem that a corporation's budgets and internal earnings forecasts would come within the scope of the carve-out included in the rule and do not therefore have to be disclosed. Market practice supports this view. The s 1022AA regime attempts to deal with this through subs (6), which provides as follows:

> "1022AA(6) [Information to be included in prospectus] If:
> (a) there is information relating to the disclosing entity that has not, because of its confidential or prejudicial nature:
> (i) been notified to a securities exchange under provisions of the securities exchange's listing rules referred to in subsection 1001A(1); or
> (ii) been included in a document lodged under section 1001B; and

[11] Corporate Law Reform Bill 1993 (Cth), Explanatory Memorandum, Sched I.

(b) investors and their professional advisers would reasonably require the information, and would reasonably expect to find it in the prospectus, for the purpose of making an informed assessment of:
 (i) the assets and liabilities, financial position and prospects of the disclosing entity; and
 (ii) the rights attaching to the securities;
the information must be included in the prospectus."

This effectively means that if there is information in such budgets and forecasts which has not been disclosed to the market in reliance on the carve-out under Listing Rule 3.1 but which investors and their professional advisers would reasonably require and would reasonably expect to find in a prospectus for the purpose of making an informed assessment of the prospects of the issuing corporation, then such information must be included in a prospectus issued under s 1022AA.

Against this background the apparently conflicting decisions of the Federal Court in *Pancontinental Mining Ltd v Goldfields Ltd*[12] and the Supreme Court of New South Wales in *Solomon Pacific Resources NL v Acacia Resources Ltd*[13] fall to be considered.

Both cases involve scrip bids in respect of which the target took proceedings to restrain the dispatch of the relevant Pt A Statement and accompanying offers because of alleged deficiencies in the Pt A Statement. The deficiencies alleged in each case included a failure on the part of the offeror to include an earnings forecast in the Pt A Statement.

The facts of the Pancontinental case may be set out briefly as follows. Goldfields Ltd (Goldfields) served a Pt A Statement on Pancontinental Mining Ltd (Pancon) pursuant to which it proposed to make takeover offers under a takeover scheme for all the issued shares in Pancon. The consideration to be offered was one Goldfields share plus $2.10 cash for every three Pancon shares. Goldfields was not listed on the ASX. Pancon sought orders and declarations that the Pt A Statement did not comply with the Law and that Goldfields be restrained as a consequence from despatching offers.

It was argued by Pancon that in order to satisfy the requirements of cl 17 of Pt A of s 750 the Pt A Statement must include either a discounted net present value of the future cash flows of the post-acquisition assets of Goldfields or an earnings forecast.

In arriving at his decision, Tamberlin J was able to derive some general guidelines from earlier relevant decisions, some of which are set out below:

"1. Materiality is a question for the court although evidence may be tendered to enable the court to understand why certain matters are material or why they are not: *ICAL Ltd v County Natwest Securities Aust Ltd* (1988) 13 ACLR 129 at 137. It is a question of mixed fact and law and it depends on the facts and is to be determined on a case-by-case basis ...

[12] (1995) 16 ACSR 463.
[13] (1996) 19 ACSR 238.

6. The object is to put shareholders in possession of the information required to enable them to make an informed and critical assessment of the offer and an informed decision whether to accept it. Information is material which could affect the shareholders' assessment of whether the offeror is likely to improve its offer, the prospects of a competing offer, and the prospects of the shares if retained. A relevant question is whether the information would assist shareholders to assess critically the attractiveness of the offer ...
11. Finally, the Part A statement must be read fairly as a whole and not in discrete parts or selectively."[14]

The expert evidence in the case was conflicting. The expert witness called by Pancon gave evidence that one or both of a discounted net present value of the future cash flows of the Goldfields assets or an earnings forecast post-acquisition are necessary to enable a proper decision to be made on whether to accept the offer, and in order to make an assessment of the prospects of Goldfields. This was said to be all the more necessary because Goldfields had no "track record" in the market or any earnings history. An affidavit by the expert witness exhibited eight recent prospectuses issued in the prior two-year period by producing mining companies. In all eight prospectuses there were earnings forecasts — four for a one-year period and four for a two-year period. In one prospectus there was also a Discounted Cash Flow (DCF) analysis.

The evidence of the expert witness called by Goldfields was that it would be helpful but not essential to have either or both a DCF analysis or a forecast of Goldfields earnings in order to value Goldfields shares post-acquisition. The expert conceded that he was not aware of any recent initial public offering of shares in a new mining company which did not include an earnings forecast however he said that not all the information necessary to enable Goldfields to put together an earnings forecast was publicly available.

The central finding of his Honour is set out below:

"However, I am of the view that Pancontinental and its offeree shareholders are entitled under the Law to the benefit of an earnings forecast over, at least, a two year period. The fact that each of the recent eight mining company prospectuses, referred to by Mr Duffin, contain earnings forecasts supports the view that such forecasts are material information and are regarded as such by mining companies and their advisers. Such a forecast would be likely to be of real and material assistance to show offerees what they may receive. Even if it is based on a number of assumptions, these assumptions and qualifications can be spelt out as was done for example in the ... prospectuses exhibited to the affidavit of Mr Duffin" (emphasis added).[15]

[14] (1995) 16 ACSR 463 at 466-468.
[15] Ibid at 471.

This finding led to the conclusion that the lack of an earnings forecast had the result that the Pt A Statement did not comply with the requirements of either cl 17 or cl 18 of Pt A of s 750. His Honour pointed out that his finding did not mean that an earnings forecast is essential under s 750 in every case as a matter of law.

However, notwithstanding that caveat it would appear to the writer that the omission of an earnings forecast from a Pt A Statement relating to a scrip bid is something that should be approached with great caution.

The findings in the *Pancontinental* case meant that the court rejected arguments that the inclusion of an earnings forecast in the Pt A Statement was not necessary because:

(a) the offeror had insufficient information on which to base such an earnings forecast and therefore such a forecast would be misleading; and

(b) other financial information sufficient to enable an investment adviser to form an informed opinion as to the prospects of the offeror had been included throughout the Pt A Statement.

In dealing with the last point, his Honour said:

> "An offeree, when faced with a complex and lengthy prospectus, such as the present document, should not have to forage through the whole prospectus, seeking out fragments of information in order to piece together the assumptions and construct a forecast of earnings from a number of disparate and indirect scattered references in a 250-page document. If the information is there the offeror should perform the exercise and not leave it to the offeree to make assumptions. Such a forecast by Goldfields would affect any decision whether to accept the offer or seek a higher price. The offeree is entitled to have the forecast clearly set out, in a lucid and direct form, in a prominent part of the statement, so that attention can be focused on the critical matter of earning potential. Not every offeree will have a sophisticated investment consultant at hand when perusing the statement to perform these arcane exercises" (emphasis added).[16]

The conclusion that the Pt A Statement did not comply with the requirements of cl 17 because of the omission of an earnings forecast requires careful consideration. It is easy to see that the requirements of cl 18 will vary significantly depending upon whether the offer consideration includes quoted ED securities on the one hand (thereby necessitating compliance with the s 1022AA prospectus requirements) or unlisted securities (thereby necessitating compliance with the s 1022 prospectus requirements) on the other. It is, however, in the writer's opinion by no means clear that an "earnings forecast" ceases to be material information for the purposes of cl 17 just because the securities to be issued as part of the offer consideration are quoted ED securities. There is no obvious reason why in such circumstances an earnings forecast ceases to be "of real and material assistance to show offerees what they may receive".

[16] Ibid at 472.

It is of course true that at any particular time there are usually analysts' estimates of future earnings of listed corporations to which offerees and their advisers might refer in the event that they receive takeover offers from a listed corporation involving a scrip consideration. But even if these estimates were reliable, which they may not be, they will not in most cases afford an offeree any basis upon which to assess "the critical matter of earning potential". This is because the post-takeover earnings of the offeror will usually include earnings from the target adjusted to take account of asset sales and rationalisation benefits. As noted earlier the offeror will invariably have undertaken a detailed financial analysis of the takeover, including compilation of earnings and cash flow forecasts, prior to deciding to proceed with the bid, and it is difficult to see a convincing reason why this is information which should not be disclosed to satisfy the requirements of cl 17.

In *Solomon Pacific Resources NL v Acacia Resources Ltd* McLelland CJ of the Equity Division of the Supreme Court of New South Wales approached "earnings forecasts" in a different way.

In this case Acacia Resources Ltd (Acacia) made a scrip bid for Solomon Pacific Resources NL (Solpac). Solpac applied to the court for an injunction restraining the dispatch of offers to its shareholders based on the alleged invalidity of the Pt A Statement. The grounds for challenging the Pt A Statement included the lack of any information in the Pt A Statement in the nature of earnings forecasts or cash flow projections for Acacia. It was argued, apparently without reference to the *Pancontinental* case, that such information was necessary to enable Solpac shareholders to assess the financial prospects of Acacia, including its prospects for future growth and expansion. Such information was said to be "material to the making of a decision by an offeree on whether or not to accept the offer" and accordingly it was argued that the omission of such material resulted in a breach of cl 17.

In dealing with these arguments his Honour observed:

> "In my view, there is for present purposes a significant distinction to be drawn between facts and predictions. Predictions, whether in the form of forecasts or projections or in any other form, are inherently speculative and subject to contingencies of varying degrees of probability and foreseeability. The very inclusion in a Part A statement of such a prediction might well be potentially misleading. There is no evidence as to what earnings forecasts or cash flow projections might exist or how reliable they might be. I am not persuaded that this alleged deficiency is sufficiently clear or significant to justify the grant of an interlocutory injunction."[17]

The suggestion that the omission of earnings forecasts from the Pt A Statement is justified because such forecasts are predictions as to future occurrences which may not come to pass and are therefore potentially misleading is, with respect, hard to accept. Any suggestion that cl 17 does not

[17] (1996) 19 ACSR 238 at 242.

apply because the offeror cannot be shown to have prepared an earnings forecast is also hard to accept and flies in the face of commercial reality because as noted earlier it is scarcely credible that an offeror would not have prepared earnings forecasts in the process of deciding whether or not to bid. Such an approach would also be at odds with the willingness of the courts to infer the existence of information relevant to the offeror's intentions.

In the writer's submission the better view is that any inherent uncertainty in earnings or cash flow forecasts can be appropriately dealt with by setting out the assumptions on which the forecasts are made and attaching appropriate qualifications rather than by omitting such forecasts. It is submitted that this is supported by the current market practice in relation to prospectuses where if his Honour's view were correct it would follow that earnings forecasts need not be included as they might render the prospectus potentially misleading.

The approach advocated is also supported by obiter in the *Pancontinental* case where Tamberlin J observed:

> "Of course, some assumptions will have to be made, but they can be readily stated and cautionary warnings sounded as to the order of accuracy or dangers inherent in such an earning and dividend forecast."[18]
>
> "Qualifications and assumptions can be set out by the offeror to explain or qualify the forecast as has been done in the prospectuses exhibited. It is clearly of importance for a shareholder to have the benefit of the offeror's estimate as to future earnings."[19]

This residual uncertainty will, in the writer's opinion, continue the existing market bias against scrip bids.

COMPULSORY ACQUISITION AND SHARE-SPLITTING

In the last few years we have seen some interesting attempts at preventing offerors from utilising the compulsory acquisition provisions of Ch 6 of the Law. In the course of one of these attempts shareholders in a target company have been offered free shares and even a free ham, causing litigation in the matter to be dubbed "the Ham Scam case".

Section 701 of the Law provides a mechanism which enables successful offerors to compulsorily acquire the shares of a dissenting offeree if certain conditions are satisfied. If an offeror is entitled to less than 10 per cent of the shares to be acquired in the target at the commencement of the bid it need only become entitled to 90 per cent of such shares during the takeover period in order to be able to utilise the compulsory acquisition procedure.

[18] (1996) 16 ACSR 463 at 472.
[19] Ibid.

If at the commencement of the bid the offeree is already entitled to more than 10 per cent of the shares to be acquired then the offeror must in addition to becoming entitled to 90 per cent of the shares during the takeover period, either:

(a) acquire the shares held by three-quarters of the offerees (whether pursuant to its offers or otherwise); or
(b) be in the position that three-quarters of the persons who were registered holders of shares on the day the Pt A Statement was served on the target company are not so registered at the end of one month following the end of the offer period.

The first of these requirements gives rise to an "acceptance test" and the second gives rise to a "departure test".

Companies associated with John Thompson (a resident of New Zealand) have sought in a number of takeovers to frustrate the ability of offerors to utilise the compulsory acquisition procedures in a number of different ways.

The first of these was a bid by Homestake Mining Co (Homestake) to acquire the shares it did not own in Homestake Gold Australia Ltd (HGAL). On 14 August 1995 Homestake announced its intention to make takeover offers for the outstanding shares in HGAL. At that time HGAL was entitled to in excess of 80 per cent of the shares in HGAL and Peninsula Gold Pty Ltd (Peninsula), a company controlled by Thompson and holding 95,000 shares in HGAL. On 16 October 1995, the solicitors for Peninsula wrote to the HGAL share registry requesting the registration of 918 share transfers each for 100 shares to third parties. The transferees agreed that Thompson would pay all costs incurred in relation to the transfers and that he would retain effective control of the shares following registration of the transfers in favour of the transferees.

On 10 November 1995 Thompson wrote with an offer of 50 free HGAL shares to those persons who were registered as HGAL shareholders on the day before Homestake served its Pt A Statement on HGAL. It did not matter that the offerees might have already sold their HGAL shareholdings to Homestake. The offer was subject to a number of conditions which were aimed at seeing that Homestake would be unable to satisfy the "departure test" upon completion of its bid. In a subsequent letter, apparently signed by "John L (Father Christmas) Thompson", a succulent cooked leg ham was offered as an added inducement to those persons who accepted the offer by 20 December 1995.

The response of Homestake to Thompson's share-splitting scheme was to apply to the ASC for a modification of the provisions of s 701 pursuant to the powers conferred by s 730 of the Law. The ASC granted the modification and Peninsula, with Thompson, appealed to the Administrative Appeals Tribunal against the granting of the modification.

Peninsula argued that:

(a) the *Corporations Law* does not prohibit share-splitting;
(b) the modification affected private property rights of the transferees in a way not authorised or contemplated under s 730;

(c) the modification resulted in the expropriation of minority shareholders in a way that was *contrary to the proper purpose and fairness principles as determined by the High Court in Gambotto v WCP Ltd*;[20] and

(d) there was no evidence and accordingly no proper basis upon which to conclude that the applicants were intending to "greenmail" Homestake.

McDonald DP distinguished *Gambotto* on the basis that the provisions of Ch 6 expressly address the balance between protecting the interests of minority shareholders and promoting a company's ability to compulsorily acquire shares.

The tribunal noted that in granting a modification under s 730 the ASC was obliged to have regard to the so-called "Eggleston principles" contained in s 731 and in particular to the requirement that the ASC exercise its powers so that, as far as practicable, all shareholders of a company have a reasonable and equal opportunity to participate in any benefits of a takeover.

In summing up the effect of the share-splitting arrangements McDonald DP said:

> "The tribunal is satisfied that he [Thompson] has gained by the share-splitting a tactical advantage over other HGAL shareholders which gives him the opportunity, whether he chooses to use it or not, of negotiating an advantageous position after the close of the offer period with the offeror which he would not have enjoyed if the share-splitting had not occurred. By virtue of the agreement with the transferees, Mr Thompson stood to reap any benefit from an increased offer because he controlled whether the test in s 701(2)(c)(i) [the acceptance test] could be met by the offeror or not."[21]

The tribunal accepted that the arrangements were artificial and concluded that:

> "To that extent other offerees who had accepted the offer during the offer period were not extended a 'reasonable and equal' opportunity to participate in the benefits (contrary to the provisions of s 731(d)). That, in the view of the tribunal, is an act contrary to the general principles outlined above. The [ASC] overcame the circumstances which gave Mr Thompson that potential advantage by its modification of s 701(2)(c)(i) and returned the status quo so that the share registry reflected his true position as the beneficial owner of shares the subject of the share-splitting scheme as if that scheme had not occurred. Having regard to the provisions of s 731(d), that was, in the view of the tribunal, the correct action for the [ASC] to take."[22]

[20] (1995) 182 CLR 432.
[21] (1996) 19 ACSR 703 at 714-715.
[22] Ibid at 715.

The tribunal decided that the modification granted in respect of the "departure test" should also be sustained on a similar basis. The tribunal rejected the other grounds for review advanced by the applicants. The ASC subsequently issued Media Release 96/92 referring to the decision in the *Homestake* case, encouraging companies to watch for signs of share-splitting and indicating that it would favourably consider any application for modification of the Law to counteract the effect of such share-splitting practices.

A lack of success in the Ham Scam case left Thompson undeterred judging by the proceedings in some further litigation in which he was involved.

The relevant facts are that on 15 April 1996 GUD Holdings Ltd served a Pt A Statement on Sunbeam Victa Holdings Ltd (Sunbeam Victa). On 18 April 1996, Thompson caused 1,158 transfers between himself and 18 others (including Peninsula) to be lodged for registration by Sunbeam Victa.

There were delays in registering the transfers due to the transfers being inadequately stamped and Sunbeam Victa applying to the ASX for the waiver of a Listing Rule obliging it to register the transfers within five days after lodgement of a registrable transfer. The waiver was refused and an appeal to the ASX National Listing Committee was rejected. The transfers were subsequently registered on 24 May 1996.

Peninsula, Thompson and others took proceedings in the Supreme Court of New South Wales[23] seeking registration of the share transfers which had been registered by the time the matter came before the court. Thompson and the other plaintiffs continued the proceedings seeking declarations that the share register should reflect that the effective date of registration of the relevant share transfers should have been 8 May 1996 (being the last day by which Sunbeam Victa should have registered the transfers in accordance with the Listing Rules) rather than 24 May 1996 being the actual date of registration.

Bryson J, in rejecting the plaintiff's submissions, said:

> "Sunbeam was confronted with very strange behaviour by Peninsula and its numerous combinations of transferees and, while to many minds it would seem that it was not useful to resist this behaviour, it was fully within the range of reasonable consideration to decide to seek a waiver from acting on it. If some practical advantage which the court ought to protect flows to the plaintiffs from the course which they have taken it has not been revealed. If some practical disadvantage has not been imposed on the plaintiffs by the delay in registration that too has not been revealed. The relief sought is discretionary, yet I am asked to grant it without being told any substantial reason why the grant of it would improve the position of the plaintiffs."[24]

[23] *Peninsula Gold Pty Ltd v Sunbeam Victa Holdings Ltd* (1996) 20 ACSR 553.
[24] Ibid at 559.

Thompson was not telling the court the nature of the advantage he was seeking and the court was not responsive.

When the share-splitting became evident both Sunbeam Victa and GUD made applications to the ASC for a modification of s 701 such that the share-splitting would not frustrate use of the compulsory acquisition procedures. Thompson took action to restrain the ASC from granting the modification.

In the proceedings[25] Thompson argued that s 730 confers power on the ASC to modify or alter the way in which the relevant provisions of the Law operate, but not to modify or alter the substantive law as it affects individual rights.

McLelland CJ (in Equity) found that:

> "A declaration of the kind in contemplation would not effect any substantive alteration to the general law: the power of a shareholder to split its holding or otherwise deal with its shares and any exercise of that power, would remain lawful and effective. All that would be changed is the effect of s 701 on the state of affairs resulting from particular instances of such dealings designed to frustrate the policy of the legislation. Such changes are in my view well within the intended reach of s 730."[26]

In the writer's opinion the decisions referred to above were all correctly decided. It would be a most unfortunate development in Australian securities markets if such blatantly artificial devices could be used by an individual like the imaginative Thompson to procure a commercial advantage for himself. The ASC is to be commended for its initiative and willingness to overcome such practices.

Thompson is, however, persistent and has recently been involved in proceedings in relation to the Grundy takeover of Sea-FM Ltd. In the writer's opinion it is to be hoped that the judgment in these proceedings, which is still awaited, offers Thompson no encouragement to continue his share-splitting ways.

CONCLUSION

Because of the magnitude of the commercial interests involved, unwelcome takeover bids will continue to generate litigation. Much of the litigation is likely to involve issues as to whether the offeror has made adequate disclosure in the bid documentation. The cases referred to in this paper provide guidance to those preparing the bid documentation but confirm that the sufficiency of disclosure is a matter to be considered on a case by case basis. There remain unresolved issues as to the inclusion of earnings forecasts in Pt A Statements prepared in connection with scrip bids which are likely to continue to have the result that scrip bids are used infrequently.

[25] (1996) 21 ACSR 246.
[26] Ibid at 250.