LEGAL COMMITTEE
OF THE
COMPANIES AND SECURITIES ADVISORY COMMITTEE

ANOMALIES IN THE TAKEOVERS PROVISIONS OF THE CORPORATIONS LAW

DISCUSSION PAPER

JANUARY 1993

Introduction

Background

This Discussion Paper has been prepared by the Legal Committee of the Companies and Securities Advisory Committee and approved for publication by the Advisory Committee.

The present Legal Committee was established in September 1991. Its function is to provide expert analysis, assessment and advice to the Advisory Committee in relation to matters referred to it by that Committee connected with:

(a) a proposal to make or amend a national scheme law;

(b) the operation or administration of a national scheme law;

(c) law reform in relation to a national scheme law;

(d) companies, securities or the futures industry; or

(e) a proposal for improving the efficiency of the securities markets or futures markets.

Membership of the Advisory Committee

The members of the Advisory Committee are:

Mark Burrows (Convenor) - Baring Brothers Burrows & Co Limited

Don Argus (Deputy Convenor)- National Australia Bank Limited

John Barner- Coles Myer Ltd

Reg Barrett - Westpac Banking Corporation

Professor Philip Brown - University of Western Australia

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Membership of the Legal Committee

The members of the Legal Committee are:

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James Douglas QC- Barrister, Queensland

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Geoff Hone- Blake Dawson Waldron

Marie McDonald- Blake Dawson Waldron

Kim Santow- Freehill Hollingdale & Page

Valentine Smith- Dobson, Mitchell & Allport

Malcolm Starr - International Banks and Securities Association of Australia

Barbara Whittle- Clayton Utz.

The members of the Legal Committee were assisted in the preparation of the Discussion Paper by Vincent Jewell and John Kluver of the Advisory Committee Executive. The Legal Committee also wishes to acknowledge the assistance

given by George Durbridge, General Counsel of the Australian Securities Commission, and by James Lonie, Legal Officer of the ASC, in making suggestions for law reform and in developing specific proposals for reform.

Objective of the Discussion Paper

This Discussion Paper constitutes the first major review of takeovers legislation since the Companies (Acquisition of Shares) Act and Codes (CASA) were enacted by the Commonwealth and the States in 1980. Aspects of the takeover law have been reviewed by the Companies and Securities Law Review Committee in its reports, Report on the Takeover Threshold (November 1984) and Report on Partial Takeover Bids (August 1985). The purpose of the Discussion Paper is to simplify and streamline the takeovers provisions by identifying anomalies that have become apparent in the practical application of Chapter 6 (Acquisition of Shares) and related provisions in Part 1.2 (Interpretation) of the Corporations Law and suggesting measures to remedy those anomalies. The Legal Committee has not addressed the general policies underlying those provisions except where necessary to formulate proposals to deal with anomalies.

Several of the Legal Committee's proposals include draft amendments to the Corporations Law. The Legal Committee does not generally consider legislative drafting to be one of its functions. However, it believes that, in some instances, its proposals may be better assessed if draft amendments are suggested.

Structure of the Discussion Paper

Part 1 of the Paper examines several problems that arise from the concepts of power to vote and dispose, 'relevant interest' and 'entitlement', as used in the Corporations Law to describe control over shares. In particular, it examines the difficulties in the operation of those provisions which trace a company's power over shares to persons who hold significant shareholdings in that company. The anomalous consequences that may follow from the definition of 'acquire' when non-voting shares are converted into voting shares are also considered.

In Part 2, the Legal Committee discusses anomalies in relation to the exceptions to the prohibition on the acquisition of shares in s 615. The topics discussed are:

* difficulties caused by the formula in s 618 providing for acquisitions of 3% of a company's shares every six months

* amending s 618 to take into account the downstream consequences of 3% acquisitions

* the limitation to proprietary companies of acquisitions of shares with the consent of members (s 619(1)(b))

* the exception in section 621 for pari passu allotments, as it applies to foreign shareholders

* acquisitions pursuant to a prospectus (s 622(1))

* agreements to purchase shares that are conditional on the approval of shareholders under s 623

* the restriction of s 623 to acquisitions by purchase or allotment

* acquisitions pursuant to a compromise or arrangement (s 625)

* the extension to other convertible securities of the exception for acquisitions pursuant to renounceable options and convertible notes (s 627)

* the exception for certain downstream acquisitions (s 629).

Part 3 deals with a variety of procedural and miscellaneous matters relating to takeover schemes and takeover announcements under Chapter 6. It includes such matters as the formal requirements for offers, timing requirements, offer conditions and the prohibition on giving certain benefits to particular shareholders.

This Paper does not deal with anomalies arising under the compulsory acquisition provisions in Pt 6.5 Div 6. These may be the subject of a separate Discussion Paper.

Unless otherwise indicated, all references in the Discussion Paper are to sections of the Corporations Law.

Submissions sought

The Legal Committee seeks submissions on the matters raised by this Paper, and any other anomalies that have been encountered in the operation of Chapter 6 and related provisions in Part 1.2.

The address for submissions is:

Takeovers Review

Companies and Securities Advisory Committee

GPO Box 4866

SYDNEY NSW 2001.

Closing date: **Friday 23 April 1993**

Part 1. Concepts of control: power, relevant interests and entitlements

Addition of the words 'or an associate of the body corporate' in s 33

Section 33 traces to a person the power that a body corporate or an associate of the body corporate can exercise in relation to shares. CASA s9(5), the

predecessor of s 33, only traced the power of the body corporate itself, not the power of an associate of the body corporate. The Explanatory Memorandum to the Corporations Bill 1988 acknowledged (without explanation) that s 33 extended CASA s 9(5).

As presently drafted, s 33 has various anomalous effects:

* there is an inconsistency between its terms and the operation of s 609[1]

* unlike CASA, it deems an associate of the body corporate to have a relevant interest in, not merely an entitlement to, shares, thereby considerably extending its ambit[2]

It has been suggested to the Legal Committee that s 33 has been expanded by adding a reference to 'an associate of the body corporate' so that the power of a director of the body corporate (being 'the associate') is traced back to 'the person[3]. The Legal Committee considers, however, that the power of the director should be traced back to 'the person' only if the director and 'the person'

1. For example, assume that a body corporate A has an associate B which holds a relevant interest in 20% of the shares in company C. A and B are associates because they have entered into an agreement under which A is to purchase half of B's shareholding in C (s 12((1)(f)). Under s 609, A is only entitled to the shares to which the agreement relates, that is 10%o of the shares in C. Assume that a person P holds 20% of the shares in A. Section 33 provides that where an associate (B) of a body corporate (A) has power to vote or dispose of shares (in C), a person (P) shall be deemed to have in relation to the shares in C the same power as the body corporate (A) or the associate (B) has ff the person (P) has power to vote in respect of not less than the prescribed percentage (20%) of the voting shares in the body corporate (A). Thus P is deemed to have B's relevant interest in 20% of the shares in C whereas A only has an entitlement to 10% of the shares in C. This is significant for two reasons. The first is the difference between the percentage relevant interest of P and the percentage entitlement of A. The second is the fact that A's deemed interest is an entitlement while P's deemed interest is a relevant interest: this aspect is s~ in footnote 2.

2. The difference in effect between relevant interest and entitlement can be seen from the facts in footnote 1. A person who becomes associated with P other than by reason of s 12(1)(d), (f) or (g) will have an entitlement to 20% of the shares in C since P is deemed to have a relevant interest in the shares in C yet a person who becomes associated with A will have no deemed interest at all since A only has an entitlement.

3. For example, company W holds 20% of the shares in company X. Z, a director of X, holds 10% of the shares in company Y. W also holds 10% of the shares in Y. W and Z voting together control 20% of the votes in Y. The effect of s 33, as presently drafted, would be automatically to deem W to have a relevant interest in the 10% shareholding of Z in Y.

are, in fact, associates (which is to be determined pursuant to the associates provisions in Pt 1.2 Div 2).[4]

The creation of artificially broad relevant interests by s 33 constitutes an unwarranted impediment to commercial transactions. It is unnecessary given the terms of Pt 1.2 Div 2, and in its current form may even afford scope for the avoidance of Chapter 6 in some circumstances.[5]

Proposal 1: The words 'or an associate of a body corporate' should be removed from the introductory words of s 33 and the words 'or associate' should be removed from the part of the section between s 33(b) and (c).

Use of the phrase '(other than this section)' in s 33

In 1985, the predecessor of s 33 was amended by adding the words '(other than this section)'. The amendment was intended to prevent the provision having an over-reaching effect in consequence of deeming control through a chain of minority shareholdings[6]. One commentary has suggested that the amendment did not achieve its purpose of exempting minority holdings.[7] The remedy proposed in

4. To take the facts of footnote 3, if W and Z are acting in concert or there is some agreement, arrangement or understanding between them under which W may influence the way Z votes or disposes of its shares in Y, W and Z will be regarded as 'associates' for the purpose of Pt 1.2 Div 2. Depending on the nature of their relationship, W would then be entitled to some or all of the shares held by Z in Y pursuant to s 609. In the Legal Committee's view, it is appropriate that Z's voting power only be traced back to W where such an association in fact exists. The width of s 33 can also be demonstrated by noting that ff W was not itself a company, but was a person who was a director of another company, P for example, P would then be regarded as entitled to all of the shares in which W had a relevant interest, 'including those shares held by Z in Y.

5. For example, to take the facts of footnote 3, W could subsequently proceed to purchase any shares held by Z in Y, even where Z held 20% of the shares in Y. W's entitlement to shares in Y would not thereby increase and a contravention of the Corporations Law would only occur ff there was a flow-on increase in some other person's entitlement to shares in Y.

6. Before the amendment, the CASA equivalent of s 32 and 33 was s 9(4). The amendment split the provision into two subsections; the new s 9(5) contained the tracing power that relied on holdings of more than the prescribed percentage of shares in a company. The Explanatory Memorandum to the Bill that contained the amendment said that '[u]nlike CASA s-sec. 9(4), proposed s-sec. 9(5) will not have an extended operation, i.e. a person will not be deemed to have control of Company B if he controls 20% of Company A which controls 20% of Company B even though Company A is deemed to have control of Company B)'.

7. Renard & Santamaria, Takeovers and Reconstructions in Australia, para 416. This can be illustrated by the following example:

A Ltd --> 20% --> B Ltd --> 49% --> C Ltd --> 100% --> D Ltd

Assume that C is the body corporate first referred to in s 33 and A is the person referred to between paragraphs 0') and (c) of s 33.

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the commentary was to move the words '(other than this section)' from where they are now to follow the word 'Division' between s 33(b) and (c). However, this does not provide a complete solution.[8] The Legal Committee believes that to avoid tracing through minority shareholdings, the following amendment to s 33 is required.

Proposal 2: The words '(other than this section)' should be left where they appear in s 33 and should be repeated after the word 'Division' appearing between s 33(b) and (c).[9]

C has power to vote and dispose of 100% of the shares in D, as required by s 33(a) and (b). This power arises directly and not by a deeming provision of the Division. Thus the words '(other than this section)' do not apply.

A has the same power as C has over the 100% shareholding in D for the following reasons:

(1) A has power to vote in relation to not less than 20% of B which has power to vote in relation to 49% of the shares in C

(2) A is deemed by s 33 to have power to vote in relation to B's 49% shareholding in C

(3) s 33 says that A (the 'person') shall be deemed to have the same power to vote and dispose that C (the 'body corporate') has if A has the power to vote in respect of not less than the prescribed percentage (20%) of the voting shares in C

(4) A is deemed by the previous application of s 33 described in step (2) to have, for the purposes of Pt 12 Div 5 (which includes s 33), the power to control not less than 20% of the shares of C as required by step (3)

(5) A therefore has C's power in relation to 100% of the shares in D and s 33 has a successive effect notwithstanding the words '(other than this section)' which appear in the wrong place for the purpose of the example described.

8. Assume the same facts as in footnote 7, and apply the section from the perspective of B being the 'body corporate' and A being the 'person' in s 33.

** B is deemed by s 33 to have power to control the voting and disposal of C's 100% holding in D because B has 49% of the shares in C, which is more than the prescribed percentage*

(20%).

** If the words '(other than this section)' are moved from the opening words of s 33 as suggested, this power of B can be taken into account in giving further effect to s 33.*

** Under s 33, A (the 'person') shall be deemed to have the same power as B (the 'body corporate') has or is deemed to have in relation to the 100% shareholding of C in D because A has the power to control not less than 20% of the voting shares of B.*

** A's power over the shares in B would be disregarded if it were a power that is deemed to arise under s 33. However, the power of A over 20% of the shares in B is real and does not depend on the previous application of s 33.*

** Therefore deleting the words '(other than this section)' from where they currently appear in s 33 would continue to permit s 33 to have a successive effect.*

9. Assume the same facts as in footnote 7. Having the words '(other than this section)' in both prices will mean that neither of the problems described in footnotes 7 and 8 will arise. Inserting the words after 'Division' will prevent A from having the power to vote in respect of not less than the prescribed percentage (20%) of the voting shares in C as required by s 33(c), as pointed out in footnote 7. Keeping the words where they currently appear will prevent A from being deemed to have B's power in relation to the shareholding of C in D since B's power is deemed by a previous operation of s 33, as pointed out in footnote 8.

Sections 32 and 33 and the exceptions in s 38 to s 43

Sections 38 to 43 are intended to recognise that certain persons with particular types of interests in shares (for example, persons whose ordinary business includes lending money) should not be regarded as having control over the shares for the purpose of the Corporations Law. However, these provisions do not fully take into account the deeming effect of s 32 and s 33[10] for the following reasons.

* Sections 32 and 33 are expressed in terms of powers to vote and dispose, rather than relevant interests. The instruction in s 38 to s 43 to ignore certain relevant interests is not expressed in terms consistent with s 32 and s 33.

* The exceptions in s 38 to s 43 focus on characteristics of the person whose relevant interest is to be disregarded rather than characteristics of another person through whom the relevant interest is derived,[11]

The Legal Committee considers that a basic rule of interpretation should be added to the Corporations Law to make it clear that

* relevant interests should not be distinguished from the power to vote in respect of, or to dispose of, a share that constitutes the relevant interest in determining whether the provisions for disregarding relevant interests apply and

* a person's relevant interest will be disregarded if the relevant interest of the person through whom it was derived would be disregarded.

Proposal 3: A new s 31(3) should be added to the Corporations Law to the following effect:
"Where a relevant interest of a person in a share is required by this Division to be disregarded, the power of the person to vote in respect of the share or the power to dispose of the share which gives the person that relevant interest in the share under subsection (1) or (2) shall be disregarded for the purpose of determining whether any person has a relevant interest in any shares.".

10. For example, company A (not a money-lender) owns more than the prescribed percentage (20%) of company B's shares. B is a money-lender. Section 38 provides that B's relevant interest in any shares it holds as security is disregarded. By virtue of s 33, A has a relevant interest in those security shares. That relevant interest is not disregarded under s 38 since, unlike B, A's ordinary business does not include money-lending.

11. Thus in the example given in footnote 10, B is the person referred to in s 38. Section 38 does not deal with a person who has more than the prescribed percentage of shares in B.

The concept of entitlement in s 609 and the exceptions in s 38 to s 43

Subsection 609(2) provides that a person, by entering into certain agreements in relation to shares, becomes entitled to those shares. This entitlement arises notwithstanding the exclusions in s 38 to s 43. For instance, the relevant interest of a money-lender in shares held as security will be disregarded under s 38. However, the money-lender will also have a separate entitlement to those shares under s 609(2)(c) which is not disregarded. Similarly, the relevant interest held by a voluntary proxy over shares will be disregarded under s 41, but the proxy holder will have a separate entitlement to those shares by virtue of s 609(2)(a).

Proposal 4: Section 609 should be amended to provide that a person's entitlement under s 609(2) shall be disregarded if the matters that give rise to the person's entitlement also give rise to a relevant interest of the person that would be disregarded under the relevant provisions of Pt 1.2 Div 5.

Section 609 as currently drafted contains a further anomaly whereby certified nominee bodies corporate may still be deemed to have an entitlement to shares of their associates.[12]

Proposal 5: Subsection 609(2) should be amended to ensure that certified nominee bodies corporate are not taken to be entitled to shares of their associates.

Exceptions for money lenders: s 38 and s 630

The Corporations Law recognizes that money-lenders may take security over shares in the ordinary course of their business. Section 38 provides for relevant interests which arise from their taking this security to be disregarded. Section 630 also exempts from s 615 acquisitions by money-lenders resulting from enforcing a security over shares. However, these provisions relate only to 'a transaction ... in connection with lending money'. This concept may be too narrow to accommodate all financing techniques, such as the granting of bill facilities.

Proposal 6: Sections 38 and 630 should be made more comprehensive by substituting words to the effect of 'provision of financial accommodation by any means' for the term 'lending money'.

12. Paragraph 609(1)(b) provides that a person is entitled to the shares of any associates of that person (unless the association only arises by virtue of s 12(1)(d), (f) or (g)) but makes an exception if the person is a nominee body corporate approved by the ASC. However, that exception is not matched by a similar exception in s 609(2). Thus an approved nominee body corporate may have an entitlement under s 609(2) where it has a relevant agreement in relation to shares. This contrasts with the position under the forerunner of s 609(2), CASA s 7(3)(b), where approved nominee bodies corporate did not have an entitlement to shares covered by the agreement.

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Conversion from non-voting to voting shares

Section 615 provides that a person 'shall not acquire shares in a company' if any person would 'immediately after the acquisition' be entitled to more than the prescribed percentage (20%) of the voting shares in the company. Subsection 51(1) sets out the only circumstances in which a person can be said to 'acquire' shares, namely when that person acquires a 'relevant interest' in shares as a result of a transaction.

Given this, a loophole exists where shares that are convertible from non-voting to voting are acquired and the rights of conversion are not immediately exercised. The loophole arises where a person

* acquires sufficient convertible shares to give the person more than the prescribed percentage (20%) of voting shares when the conversion rights are later exercised but exercises the conversion rights at a sufficient time after the acquisition that the increase in entitlement to voting shares cannot be regarded as occurring 'immediately after the acquisition'.

* The effect of s 31(2) is that the convertible shares are 'acquired' within the meaning of s 51(1) when they are first purchased.[13] At that stage s 615 does not apply as the shares are non-voting. If and when those shares are subsequently converted into voting shares, no further acquisition takes place. The prohibition in s 615 does not apply as the increase in entitlement is not 'immediately after the acquisition'.

Proposal 7: The definition of 'acquire' in s 51 should be amended so that a person is also taken to acquire shares for the purpose of Chapter 6 at the time that non-voting shares are converted to voting shares.

13. Subsection 31(2) provides that a person who has power to dispose of a share, whether voting or non-voting, has a 'relevant interest' in the share. A person who purchases convertible preference shares obtains power to dispose of them and therefore 'acquires' a relevant interest as defined in s 31(2). Subsection 51(1) deems an acquisition to have occurred when a person acquires a relevant interest.

Part 2. The exceptions to the s 615 prohibition [14]

Acquisition of not more than 3% of voting shares each six months: s 618

Different arithmetical concepts. The policy of s 618 is to allow a person to increase an entitlement by 3% in any six month period even though the acquisition would give that person or another person an entitlement to more than 20% of the voting shares in the company. The current s 618 achieves this result where there is no change in the issued share capital of the company in the relevant six month period. However, s 618 creates anomalies where there is an increase or decrease in the issued share capital during the six month period. In those circumstances, s 618 does not permit a person's entitlement to increase by the full 3% as the section is expressed in terms of numbers of shares rather than percentage entitlement.[15]

14. Some of the discussion of policy issues in relation to the exceptions to the s 615 prohibition draws on an unpublished dissertation for the degree of Master of Laws at the University of Sydney by Vincent Jewell.

15. The way s 618 works when there is an increase and decrease in capital can be illustrated by the following examples.

Example 1: A holds 50 000 shares in company B which has an issued share capital of 100 000 shares. A subscribes for an additional 3000 shares (3% of the original share capital). The value of VA1 in the formula in s 618 is 3 000 and the value of V is 100 000. Assuming that no shares have previously been acquired and none have been disposed of, the value of VA2 is zero and the value of VD is also zero. Therefore

$100 (VA1 + VA2 - VD) = 100(3000 + 0 - 0) = 3$

V 100 000

that is, it does not exceed 3 and is therefore within the terms of s 618. A is then entitled to 53 000 of the 103 000 shares in B. This only represents approximately 51.456% of the increased share capital Now that the share capital has increased, A will be able to subscribe for 90 more shares (that is, VA1 will be 90), because the value of V is now 103 000 and the value of VA2 (the number of voting share acquired in the previous six months) is 3 000 so that

100 (VA1 + VA2 - VD) = 100(90 + 3000 - 0) = 3.

V 103 000

A is then entitled to 53090 of the 103090 shares in B: this shareholding represents approximately 51.499% of the shares in B. Successive subscriptions by A will relate to fewer and fewer shares in B and A's shareholding will not approach the 53% of the shares to which A should be entitled in accordance with the policy of s 618.

Example 2: Anomalies will also occur where a company's capital base decreases as a result of a reduction of capital. For example, if

** a shareholder is entitled to 19% of the voting shares in a company*

** the shareholder acquires a further 2% of the voting shares and*

** there is then a capital reduction*

Proposal 8: Section 618 should be amended so that it is based on percentage entitlements rather than number of shares acquired. It should permit an acquisition of voting shares provided that, after the acquisition, the percentage entitlement of any person to voting shares is not greater than 3% more than the sum of
* the person's percentage entitlement six months before the acquisition and
* any increase in percentage entitlement that came about because the person took up entitlements under pari passu allotment under s 621.
To achieve this, s 618(1) and (2) should be replaced by a single subsection:
"Section 615 does not prohibit an acquisition of voting shares in a company because of the effect of the acquisition on a person's entitlement to voting shares in the company if:

(a) the person has been entitled to not less than the prescribed percentage of the voting shares in the company for a continuous period of not less than 6 months ending on the day immediately before the day on which the acquisition takes place; and
(b) the acquisition does not result in the percentage entitlement of the person to voting shares in the company increasing to a figure greater than the sum of:
(i) the person's percentage entitlement to voting shares in the company at a date six months before the acquisition;
(cont.)

the shareholder will not be able to acquire voting shares representing 1% of the reduced capital base. 'VA2' in the formula in s 618(2) is the number of voting shares acquired in the previous six months which increased the number of shares to which the shareholder was entitled. The value of VA2 will represent more than 2%, and quite possibly more than 3%, of the reduced capital base. Although the disparity between the percentage entitlement represented by the acquisition before and after the capital reduction will be offset by the fact that shares have been disposed of under the capital reduction and hence 'VD' in the formula will have a value greater than zero, the basic anomaly caused by the capital reduction will remain. The 2% acquisition is not retrospectively invalidated, but the shareholder will not be able to acquire another 1% of the shares in the company even though the shareholder's percentage entitlement to voting shares in the company after the capital reduction may only be 2% higher than the person's entitlement before the acquisition of the voting shares.

The mismatch between the s 615 prohibition (expressed in terms of percentage entitlement) and the exception in s 618 (expressed in terms of the number of voting shares acquired and disposed of and the total number of voting shares in the company) has been recognised by the Corporations Law in one respect. Section 618 excludes shares acquired pursuant to a pari passu allotment from the number of shares to be taken into account in calculating the 3% of shares that may be acquired.

(ii) any increase in the person's percentage entitlement to voting shares in the company which has taken place during that period of six months by an acquisition to which section 621 applies; and
(iii) 3%.".
Existing s 618(3) should be retained.

Downstream acquisitions. The exception in s 618 does not have a flow-on effect to consequential increases of entitlement by the acquirer or another person in

shares in another company. A person may be unable to acquire any shares pursuant to s 618 because of this limitation.[16] Elsewhere, the Legal Committee puts forward a proposal which would overcome this problem for acquirers of listed company shares. [17] However, the Legal Committee believes that consequential downstream acquisitions should be permitted under s618, regardless of the type of company involved.

Proposal 9: Section 618 should be amended to permit 3% creeping acquisitions regardless of the downstream effect of the acquisitions.

Acquisitions of shares in small companies or with the consent of the shareholders: s 619

Section 619 provides that acquisitions of shares do not breach s 615 where

* the company in which the shares are being acquired has 15 or fewer members or the company is a proprietary company and all the members consent in writing.

* The second exception allows members of a proprietary company, of whatever size, to make an informed decision not to apply Chapter 6 in respect of a particular acquisition. The Legal Committee sees no reason why the principle of unanimous shareholder consent should be confined to proprietary companies. It proposes that members of a public company may also, by unanimous consent, exclude Chapter 6 in respect of an acquisition.

16. For example, where A holds 19% of the shares in company B and B holds 25% of the shares in company C, s 618 does not permit A to acquire another 3% of the shares in B. This is because A would, by virtue of s 33, breach s 615 in relation to C by going from an entitlement of 0% of the shares in C to an entitlement of 25% of the shares in C.

17. The Legal Committee's proposal to amend s 629 to return to the law that applied under s 12(k) of CASA (see p 18) would permit an acquisition of this kind by A where B is a listed company.

Proposal 10: The words 'is a proprietary company and' should be deleted from s 619(1)(b).

Pari Passu allotment to foreign shareholders: s 621(3)

Subsection 621(3) sets out the procedure which must be followed if a pari passu allotment of shares is to qualify for the exemption granted by s 621 where it is not proposed that shares be offered directly to foreign shareholders of the relevant company.[18] Subsection 621(3) provides that, in lieu of making offers to the foreign shareholders, the company may allot the appropriate number of shares to an approved nominee who then arranges for the disposal of those shares for the benefit of the foreign shareholders.

That procedure is out of step with ASX Listing Rule 3E(11) and with current practice whereby, in the case of a renounceable issue, the nominee or trustee does not subscribe for the shares but merely disposes of the rights to acquire the shares and then distributes the proceeds (if any) to the foreign shareholders in accordance with their entitlements. The subscription procedure outlined in s 621(3) is not popular because it could lead to the nominee suffering a loss where the issue price of the shares is pitched close to the market price.

Proposal 11: Section 621 should be amended to permit a nominee of foreign shareholders to sell pari passu rights, with the proceeds to be paid to the foreign shareholders in proportion to their shareholdings. This procedure should be an alternative to that already provided by s 621(3).

Acquisition by virtue of an allotment or purchase pursuant to a prospectus: s 622(1)

Subsection 622(1) exempts from s 615 an acquisition of shares pursuant to an allotment or purchase arising from an invitation or offer in a lodged or registered prospectus.

It is unclear what policy justifies this exception. One commentator regards the exception as arising from the complementarity of the prospectus and takeover provisions.[19] He suggests that, just as a prospectus need not be issued where a takeover scheme is on foot (Corporations Regulations reg 7.12.02), so an acquisition of shares pursuant to a prospectus should be excluded from the takeover provisions. However, the policy goals of the prospectus and takeover

18. This will usually be because of the disproportionate cost of complying with applicable foreign securities laws (most notably those of the United States of America) having regard to the number of foreign shareholders.

19. N O'Bryan, 'Takeover Offers and Prospectus Requirements under the Companies Code' (1985) 3C & SLJ 3, 4.

provisions differ. The prospectus provisions are concerned only with disclosure whereas the takeover provisions serve further functions, in particular that target company shareholders have an equal opportunity to participate in benefits accruing from a person acquiring a substantial interest in the company.[20]

Even in relation to disclosure, the recipients of the information (whom the Corporations Law is intended to protect) are not the same for prospectuses and takeovers. The prospectus provisions are aimed at persons (whether or not existing members) who might acquire shares in the company. The takeover provisions are intended to assist current shareholders in deciding if they should accept the offer.[21]

In this context, it is relevant to note two other exceptions from s 615 for acquisitions of shares

* by promoters through an allotment made in accordance with a first prospectus (s 622(2)) and

* as a result of allotments made by companies that have not started any business or exercised any borrowing power (s 624).

These exceptions are appropriate since the takeover legislation is concerned with bids and acquisitions which originate after a company has been operating, not acquisitions referable to the time when the company first solicited subscription, or prior to its commencement of business.[22] In the Legal Committee's view they are adequate to cover the circumstances where a prospectus exemption is justified.

Subsection 622(1) renders s 621 superfluous given that the Corporations Law, unlike its predecessor, requires a prospectus for a rights issue. Once a prospectus has been issued, shares can simply be allotted without the need for the directors to follow the procedure set out in s 621 for a pari passu allotment.

The repeal of s 622(1) would not unduly inhibit major shareholders from subscribing for shares pursuant to a prospectus. For instance the shareholder may be permitted to acquire the shares by

* the exemption in s 618

* the exemption in s 621 for pari passu allotments (including the exemption for underwriters (see s 621(1)(b)(ii))

* shareholder approval under s 623.

Major shareholders may also be permitted to act as underwriters and acquire shares by s 622(3).

20. Section 732.

21. An offeror company may be offering shares in itself as consideration for shares in the target company, in which case its takeover documents should be a substitute for a prospectus. This is not relevant to exempting from the takeover provisions an acquisition of shares in a company as a result of a prospectus.

22. HAJ Ford & RP Austin, Principals of Corporations Law (6th edn) para 2022, p 731.

Proposal 12: Subsection 622(1) should be repealed.

Acquisition by allotment or purchase agreed to by shareholders of target company: s 623

The s 34 problem

Where a person enters into an agreement that will give that person a relevant interest in shares, s 34(a) provides that the person is deemed to have the relevant interest at the time of the agreement. Similarly, s 34(b) deems a person to have a relevant interest in a share where the person has an enforceable right in relation to the share, whether the right is enforceable presently or in the future and whether or not on the fulfillment of a condition.

These provisions create difficulties where a vendor and purchaser agree to sell shares subject to members' approval under s 623. On one interpretation of s 34, the purchaser will be taken to have immediately acquired a relevant interest and hence breached s 615 before the meeting can be held. This view was taken by Cohen J in Baden Pacific Ltd v Portreeve Pty Ltd (1988) 14 ACI. R 677.

A more pragmatic interpretation was adopted by Perry J in Magnacrete Ltd v Robert Douglas-Hill (1988) 15 ACLR 325.[23] His Honour ruled as follows.

* CASA s 9(6) (the predecessor of s 34) does not apply to an agreement which clearly contemplates that there will be no acquisition of shares until the passing of the members' resolution. The only contractual obligations which may properly be identified before the meeting are those which go to the obligation to hold the meeting.

* Alternatively, the words 'on performance of the agreement' in s 34 must be read in the context of s 623 so that if the performance of the agreement is otherwise permitted by s 623, s 34 does not operate to bring it within the s 615 prohibition.

It is doubtful whether the view of Perry J can be sustained under the Corporations Law. His Honour concluded that CASA s 9(6) permitted an agreement in which shareholder approval of a proposed allotment or purchase was a condition precedent to the creation of any obligations concerning the shares,[24] The definition in s 9 of 'relevant agreement' as used in s 34 is wider than 'agreement' as used in CASA s 9(6). 'Relevant agreement' is defined as

"an agreement, arrangement or understanding:

23. The reasoning in this case was approved by White J, with whom Molar and Millhouse JJ agreed, in Niord Pty Ltd v Adelaide Petroleum NL (1990) 2 ACSR 347, 360.

24. Refer also to NCSC Releases 116 and 348.

(a) whether formal or informal or partly formal and partly informal;

(b) whether written or oral or partly written and partly oral; and

(c) whether or not having legal or equitable force and whether or not based on legal or equitable fights".

It is probable that an agreement providing for a s 623 meeting as a condition precedent to the formation of the agreement will mount to an 'arrangement' or an 'understanding' and result in an immediate breach of s 615. Such a result is clearly contrary to the policy underlying s 623.

Proposal 13: Section 34 should be amended by adding a new subsection as follows:
"Where performance of a provision in a relevant agreement or the enforcement of a right in respect of issued shares of a company would contravene section 615, subsection (1) does not apply to the extent that the provision or right is subject to a condition that the provision shall not come into effect or the fight shall not be enforceable unless a resolution has been passed at a general meeting of the company pursuant to section 623."
Such an amendment to s 34 would require consequential changes to s 609 to state that a person does not become entitled to shares merely by virtue of entering into the agreement. Without this change, the person could subsequently acquire a relevant interest in the shares without breaching s 615 given that this acquisition did not increase the person's entitlement. In conjunction with the new subsection in s 34, a new s 609(2A) should be added to the following effect:
"A person will not be deemed to be entitled to shares under subsection (2) by reason of a provision in an agreement referred to in that subsection where the agreement is subject to a condition that the provision shall not come into effect unless a resolution has been passed at a general meeting of the company as mentioned in section 623.".

Limitation of s 623 to acquisitions by allotment or purchase

The exemption in s 623 only applies to an acquisition of shares by virtue of an allotment or purchase. It does not cover other situations where an acquisition might contravene the s615 prohibition, for example the execution of an agreement giving control over the voting or disposal of shares.[25] The Legal Committee believes that this restriction is unjustified. Shareholders should be

25. see Renard & Santamaria, op cit, para 507.

permitted to agree to any form of acquisition of a specified number of shares in their company by a particular person.[26]

Proposal 14: Section 623 should be amended to remove all reference to allotment or purchase so that shareholders can approve any acquisition of shares. In addition, s 623 should explicitly require that any resolution approved

by shareholders identify the person by whom the shares will be acquired under the agreement and the maximum number of shares to be acquired.

Acquisition pursuant to compromise or arrangement: s 625

This section exempts acquisitions pursuant to Part 5.1 from the s 615 prohibition. The exemption of acquisitions of shares 'under' a compromise or arrangement approved by the Court may not allow for all possible acquisitions which would fall within the policy of the provision.[27] The term 'under' may suggest some limitation on the application of the provision.

Proposal 15: To overcome any doubt, the words 'or by virtue of' should be added after 'under' in s 625.

Acquisition by exercise of option or right: s 627

Section 627 provides that an acquisition of shares does not breach s 615 where

* it results from the exercise of a renounceable option or an option or right conferred by a convertible note and

* an acquisition of shares at the time of the acquisition of the renounceable option or convertible note would not have contravened s615 because it would have been within the exemption for share market purchases in s 620.

26. Section 623 has already been interpreted by the New South Wales Court of Appeal in NCSC v Consolidated Gold Mining Areas NL (No 2) (1985) 9 ACLR 768 to require the approval to be for a particular person to acquire a particular number of shares. The Court required that:

** shareholders be informed of the identity of the person to whom the shares will be allotted, the number of shares to be allotted and the allottee's existing shareholding and*

** there be before the general meeting a proposed allotment and not merely a proposal to enter into some other kind of transaction which might ultimately produce an allotment.*

27. The implementation of a scheme of arrangement may involve an acquisition of shares in a company by a person who is not already a member (for example, by the creation of a new holding company). 'Inc acquisition may not be regarded as being 'under' the scheme (which is between the company and its members only) although it is contemplated in, and necessary for the effectual operation of, the scheme.

There does not appear to be any policy reason why s 627 is limited to renounceable options and convertible notes. The Legal Committee considers that this section should apply to any convertible securities.

It is also arguable that s 627 does not require the convertible securities to have been acquired in the ordinary course of stock market trading. On one reading of s 627, it is necessary only that the convertible securities be acquired at a time when s 620 would have permitted the acquirer to acquire shares. The Legal Committee considers that the requirement in s 620 that the shares be acquired in the ordinary course of stock market trading should also apply to the acquisition of convertible securities under s 627.

Proposal 16: Section 627 should be amended to
* apply to any convertible securities, not just renounceable options and convertible notes
* provide that the convertible securities must have been acquired 'at an official meeting of a stock exchange in the ordinary course of trading on the stock market of that stock exchange'.

Exception for downstream acquisitions: s 629

Outline o f s 629

Section 629 permits downstream acquisitions (that is, acquisitions of shares in one company (the downstream company) that result from the acquisition of shares in another company (the upstream company)) if

* the upstream company is incorporated in Australia and listed on the Australian Stock Exchange (s 629(a)) and

* the acquisition of shares in the upstream company results from the acceptance of an offer to acquire those shares under a takeover scheme or a takeover announcement or an acquisition under s 620 made on-market while a takeover scheme or takeover announcement is on foot (s 629(b)).

CASA s 12(k), the predecessor of s 629, only required that the upstream company be listed on the Australian Stock Exchange, not that it also be incorporated in Australia. Also, s 12(k) was not limited to acquisitions under takeover schemes or takeover announcements, but applied to any downstream acquisitions where the upstream acquisition was in a listed company. The reasons for making the exception in the Corporations Law narrower in these two respects than under CASA are obscure.

Need for exemption

The rationale for having an exemption of this type is that, where a downstream acquisition is merely incidental to the main objective of acquiring the upstream company, it should not act to fetter or inhibit the upstream acquisition, especially where the upstream company is listed. Put another way, unless the

upstream acquisition is a mere artifice, having as its true object the acquisition of the downstream company, the downstream acquisition should be exempt. Rather than articulate an exemption along these inevitably somewhat uncertain lines, the policy has been to provide a clear exemption where the upstream acquisition is in a listed company. In those circumstances, the upstream acquisition will be a serious bid (involving the acquisition of a substantial company with a large number of shareholders) and is unlikely to be an artifice to gain control of the downstream company. If the acquisition of a listed company were used as an artifice to acquire another company, the ASC could seek a declaration under s 733 that an unacceptable acquisition or unacceptable conduct had occurred.

If the bidder for the upstream company did have to bid for all downstream companies, companies could make themselves takeover-proof by holding strategic parcels of shares in a series of other companies.[28]

A further reason for exempting downstream acquisitions that result from takeovers of listed companies is that the offer price for the upstream listed company is set by the market, whereas the price that the bidder for the upstream company would have to pay for the shares in the downstream company would have to be determined by a process of valuation rather than being set by the market.

Elements o f the exemption

(i) Characteristics of the upstream company

Downstream acquisitions have only been permitted where an upstream company satisfies certain criteria.

Listing Both CASA and the Corporations Law require the upstream company to be listed in Australia. An exemption for listed companies is necessary to preserve the free market in their shares. There is not the same need in relation to unlisted companies. The Legal Committee agrees with the prerequisite of listing but would extend its application to upstream companies listed on overseas exchanges

28. Clause 1955 of the Explanatory Memorandum to the Corporations Bill 1988 said that the downstream exemption 'precludes the use of investments above the level prescribed in cl.615 as an undesirable defence tactic to a takeover of a listed company'. The possibility of using investments in this way can be illustrated by the following example. Company A holds 21% of the shares in companies B, C, D, E and F. If there were no exemption for downstream acquisitions, a person who wanted to take over company A would also need to comply with Chapter 6 in relation to companies B, C, D, E and F.

approved by the ASC. In contrast to CASA, under which exemptions for overseas exchanges were considered case by case[29], the Legal Committee proposes that

the ASC be consulted as to appropriate overseas exchanges and that these exchanges be specified in the regulations.

Incorporation in Australia. The Corporations Law requires the upstream company to be incorporated in Australia. This was not required under CASA. The Legal Committee favours the CASA approach.

The original text of the Corporations Bill 1988, like CASA s 12(k), required only that the company be 'included in the official list of a stock exchange', whether or not incorporated in Australia. The reason for including the additional incorporation requirement in s 629 may have been the Paringa case in which the upstream company was listed but not incorporated in Australia, and not subject to regulation in its country of incorporation.[30] It might be argued that the incorporation requirement in s 629 in part redresses this apparent regulatory void. The primary problem with the Paringa takeover, however, was not the downstream consequences, but the fact that the takeover of Paringa itself was not covered by any system of takeover regulation.

The Legal Committee considers that the requirement of Australian incorporation in s 629 is unduly restrictive, and not justified on the basis of one isolated instance. The requirement is also inconsistent with the proposal to include upstream companies listed on approved overseas exchanges.

(ii) Characteristics of the domain company

Neither CASA nor the Corporations Law contain criteria which the downstream company must satisfy for the exemption to apply. The Legal Committee agrees with this position.

(iii) Type of transaction

CASA did not limit the type of upstream acquisition that attracted the exemption. In contrast, the Corporations Law requires that the upstream transaction occur in the context of a takeover scheme or announcement for the upstream company or pursuant to an on-market acquisition under s 620 in the course of a takeover scheme. There was no stated policy for this additional requirement. The Supplementary Explanatory Memorandum to the

29. NCSC Release No 157.

30. Paringa Mining & Exploration Co plc (Paringa) held half the shares in North Flinders Mines. Paringa was listed in Australia. The downstream acquisition of shares in North Flinders Mines that resulted from the takeover of Paringa therefore fell within the CASA s 12(k) exception. However, Paringa was incorporated in the United Kingdom and acquisition of its shares was not regulated by CASA. Furthermore, as Paringa was domiciled in Australia, it was not subject to the City Code on Takeovers and Mergers in the United Kingdom. It was therefore not by any system of takeover regulation.

Corporations Bill 1988 simply said[31], unhelpfully, that the requirement for a nexus with a takeover bid would 'clarify and buttress the takeover provisions insofar as they apply to holding companies'. The restriction to transactions in the course of takeover schemes leaves unprotected other downstream acquisitions, for example acquisitions resulting from 3% creeping acquisitions in an upstream listed company.

The Legal Committee proposes that the Corporations Law be amended to return to the position under CASA so that a downstream acquisition that results from any upstream acquisition permitted by the Corporations Law[32] also be permitted.

Proposal 17: Section 629 should be amended
* to return to the law as it stood under CASA s 12(k) by removing the reference in s 629(a) to incorporation in Australia and the limitation in s 629(b) on the type of permitted transactions
* to extend to downstream acquisitions that result from upstream acquisitions in companies listed on overseas stock exchanges approved by the ASC.
The appropriate exchanges should, after consultation with the ASC, be prescribed by regulations.[33]
To address the problem arising from the Paringa ease, the Legal Committee would appreciate suggestions on whether s 53A should be widened to permit the ASC to declare a company incorporated overseas but having sufficient nexus with Australia to be a Chapter 6 company.

31. At paragraph 116.

32. This includes not only takeover offers and announcements but acquisitions pursuant to any of the exceptions to s 615.

33. Subparagraph Co)(viii) of the definition of 'stock exchange' in s 9 provides for bodies corporate to be declared by the regulations to be stock exchanges for the purpose of Chapter 6. However, the Legal Committee considers that it would be clearer to add a new subparagraph (b)(ix) to the definition of stock exchange, 'a stock exchange of a foreign country that is declared by the regulations to be a stock exchange for the purposes of that Chapter'. This would also obviate the need for any inquiry as to whether a particular foreign stock exchange was a body corporate.

Part 3. Takeover schemes and takeover announcements

What is the date at which shareholdings and the identity of shareholders is to be determined?

Section 635 requires that offers made under a takeover scheme relate to all (or to a fixed proportion) of the shares in the relevant class of shares held by the offeree in the target company. Subsection 636(2) requires the offeror to send an offer to each holder of shares in the relevant class. However, it is not clear whether the date for the purpose of these provisions is

* the date of service of the Part A Statement

* the date of the offers or

* the date the offers are dispatched (which is, arguably, the date they are made).

Current practice takes the relevant date to be the date of the offers? However, this interpretation leads to the following difficulties.

* Section 699 enables the offeror to request a written statement setting out the names and addresses of shareholders, convertible note holders and option holders as at the date of service of the Part A statement. If the target company changes its register between service of the Part A Statement and the dating of the offers, the offeror will have difficulty complying with s 635 and s 636(2).

* If an offeror is obliged to make offers to acquire any shares allotted between service of the Part A Statement and the dating of the offers, it would be exposed to an increase in the maximum amount of possible consideration it must provide.

* If the consideration is cash consideration, the offeror might not have arranged sufficient credit facilities to meet any increase in the consideration, and the offeror's disclosure in the Part A Statement concerning the source of any cash consideration would be inadequate.

* If the consideration includes shares, the maximum number of shares to be allotted might exceed the amount of the offeror company's unissued authorised share capital.

The Legal Committee believes that the problem could best be resolved by giving some discretion to the offeror to determine the relevant date.

34. The ASC accepts this practice notwithstanding its view that the relevant date is the date the offers are dispatched: see ASC Practice Note 7, paras 8, 12.

Proposal 18: After the word 'holds' in s 635(a) and (b), the words 'at a date stipulated by the offeror, which is not earlier than the date of service of the Part A Statement and not later than the date of the offer, being the same date in respect of each offer' should be inserted.
Proposal 19: Subsection 636(2) should be amended by adding after the word 'class':

"as at a date stipulated by the offeror, which is not earlier than the date of service of the Part A Statement and not later than the date of the offer".

Permitted differences between offers: s 636(1)(b)

Paragraph 636(1)(b) provides an exception from the requirement that offers be identical by permitting differences in the offer consideration for shares having different accrued dividend entitlements or different paid up amounts (whether by way of capital or premium).

The principle underlying s636(1)(b) is that offeree shareholders should be treated equally. The permitted differences in consideration are necessary to achieve this result. However, the formulation of the provision is deficient. It focuses only on differences in the amounts paid up and disregards differences in the amounts unpaid. The offeror's potential liability for the amounts unpaid may also be relevant in determining an offer price that achieves equality of treatment for shareholders.[35]

Proposal 20: The words 'or unpaid' should be added after the words 'paid up' in s 636(1)(b).

Requirement for offeror to send an offer to itself: s 636(2)

It is unclear whether s 636(2) requires an offeror to send an offer to itself or, in the case of a joint bid, to each offeror. Under CASA s 16(2)(c), an offeror was

35. The following example demonstrates that amounts unpaid can be relevant. An offer is made for a class of $1 shares in a company. Some of the shares have a 25(: premium, others a 50c premium (this analysis assumes that shares with different premiums do not constitute different classes of shares: refer to the discussion of Neasey J in Clements Marshall Consolidated Ltd v ENT Ltd (1988) 13 ACLR 90, 92-5). The shares are fully paid to $1, and 20c of the premium has been paid in relation to both the shares that have a 25c premium and those that have a 50c premium. There is thus no difference between the shares in relation to the amount of premium that has been paid. However the amount unpaid differs, namely, 5c and 30c respectively. An offeree would legitimately want to offer different considerations due to these differences in the amounts unpaid on the premiums.

required to send an offer to 'each holder of shares in the target company (other than the offeror) included in the relevant class of shares'. The words '(other than the offeror)' were dropped in the Corporations Law. The ASC takes the view that s 636(2) requires the offeror to send an offer to itself.[36] The Legal Committee has difficulty with this as a concept and proposes that the uncertainty that has arisen as to Parliament's intention be removed by adding to the Corporations Law the words '(other than the offeror)'.

Proposal 21: The words '(other than the offeror)' should be inserted at the end of s 636(2).

Timing

In contrast to the position under CASA, it is not permissible to serve a Part A statement on the same day it is registered.[37] CASA s 18(1) provided that a Part A statement must have been registered 'not earlier than 21 days before the Part A statement is served'. This wording permitted service on the day of registration. Subsection 644(1) requires registration 'within the 21 days ending on the day immediately before the day on which the statement is served'. Under this wording the period during which registration must take place ends the day before the statement can be served.

The Legal Committee considers that the inability to register and serve a Part A Statement on the same day is an unintended consequence of the change of wording between CASA and the Corporations Law. It was not mentioned in the Explanatory Memorandum as one of the significant changes between CASA s 18 and s 644[38]. The Legal Committee proposes that the Corporations Law be amended to remove the anomaly.

Proposal 22: The words 'the day immediately before' should be deleted from s 6440).

Payment of consideration: s 638(7)

Takeover offers must provide that the consideration for the offer is to be paid or provided not later than 21 days after the close of the offer period: s 638(7). Offer documents typically

36. Refer to ASC Practice Note 7, para 17.

37. Refer to ASC Media Release 91/104.

38. The differences between CASA s 18 and s 644 are discussed at paragraphs 2000-05 of the Explanatory Memorandum.

* reserve to the offeror a discretion to treat the receipt of an acceptance form as a valid acceptance even though the offeror does not receive the other documents necessary to establish title (such as share scrip, a power of attorney, probate or letters of administration)

* provide that the consideration will not be paid until the offeror receives all the requisite documents and all other requirements have been met.

However, there is a view that an offeror who wants to exercise a discretion to treat acceptances as valid must pay the consideration within the 21 day period under s 638(7). A requirement to pay consideration for property for which

documents of title have not been received does not accord with ordinary commercial practice. If the offeror is not willing to take the risk of paying without title, shareholders in the target company may be deprived of the opportunity to accept the offers.

Proposal 23: To overcome doubt, a new s 638(8) should be inserted as follows:
"A provision may comply with subsection (7), notwithstanding that it provides that:
(a) where an offer is accepted but documents sufficient to enable the offeror to become the holder of shares to which the offer related are not provided to the offeror with the acceptance, the consideration for the offer shall be paid or provided within:
(i) the time specified in accordance with subsection (7); or
(ii) twenty-one days after the day on which the documents are provided, whichever is the later, and
(b) the contract resulting from acceptance of the offer may be avoided at the option of the offeror if the documents are not provided within one month after the end of the offer period.".
The offeror should be permitted to rescind after one month to enable it to settle its position under s 701.

Variation of consideration under takeover offer, s 655

Section 655 sets out specific ways in which an offeror may vary the consideration specified in a takeover offer. None of these permit an offeror who has made an offer to acquire shares cure dividend to vary the offer to permit offerees to retain

the dividend[39]. The Legal Committee considers that the Law should specifically permit this variation.

Proposal 24: Section 655 should be amended by adding a new subsection (1A) to the following effect:
"Where an offeror has made an offer under a takeover scheme to acquire shares with the right to receive a dividend attached to the shares, the offeror

may vary the offer by providing that the offeree may retain all or part of the right to receive the dividend.".

Void conditions: s 662(2)

Paragraph 662(2)(b)

* prohibits a takeover offer that is subject to a defeating condition the fulfilment of which depends on a particular event that is within the sole control of the offeror or an associate of the offeror and

* makes such conditions void.

In the Legal Committee's view, the reference to an event being within the sole control of the offeror or an associate of the offeror is too narrow. Defeating conditions should be prohibited if they are within the sole control of the offeror or an associate, or associates, of the offeror or any of them together.

In one respect s 662(2)(b) is too wide. In the Legal Committee's view, defeating conditions should be prohibited only if the offeror has some ability, either by itself or through or in concert with associates, to influence whether the defeating event occurs. As presently drafted, s 662(2)(b) would apply to a defeating condition that is within the control of the target company, where the target company is an associate of the offeror by reason of being a related corporation. In such circumstances, the Legal Committee considers that it would be reasonable for the offeror to make its offers subject to defeating conditions that are within the control of the target company. Notwithstanding that the target company is a related corporation of the offeror, its directors, acting in the interests of the target company, may still cause a prescribed occurrence to occur and, in those circumstances, it is appropriate that the offeror should have the right to withdraw from its bid. Were the offeror to use its control of the target to trigger a defeating condition for the purpose of frustrating the bid in its own interest (and against the interests of the target and its shareholders), it would be subject to legal challenge, for example, under s 260 (remedy in cases of oppression) or s 733 (declaration of unacceptable conduct by the Corporations and Securities Panel).

39. The ASC agrees in principle that this type of variation should be permitted: Practice Note 4, para 7.

Proposal 25: Paragraph 662(2)(b) should be repealed and replaced with the following paragraph:
"(b) whether or not a particular event happens, being an event that is within the sole control of:
(i) the offeror;

(ii) an associate of the offeror;
(iii) associates of the offeror acting together; or
(iv) the offeror and an associate or associates of the offeror acting together.".
A new s 662(2A) should also be inserted as follows:
"A reference to an associate in paragraph (2)(b) does not include the target company or a subsidiary of the target company where the target company or the subsidiary (as the case requires) is an associate of the offeror by reason only of the operation of paragraph (b) of section 11.".

Declaration where takeover offers are conditional: s 663

Where

* conditional offers are made under a takeover scheme and

* the offers have not been declared or become free from the conditions and the conditions have not been fulfilled at the end of the offer period

all contracts resulting from the acceptance of offers and all acceptances that have not resulted in binding contracts are void: s 663(9). An offeror who intends to declare takeover offers to be free of a condition must do so not less than seven days before the last day of the offer period: s 663(2).

This requirement for early declaration may give rise to unreasonable consequences. An offeror may, for good reason, want to retain the protection of 'prescribed occurrence' conditions[40] during the final seven days of the offer period. However, s 663(2) prevents the offeror from declaring offers free from such conditions in that seven day period. The offeror risks the complete failure

40. The matters that constitute prescribed occurrences are set out in the definition of 'prescribed occurrence' in s 603 and include

** a resolution of the target company or a subsidiary for reduction of capital*

** an allotment of shares by the target company or a subsidiary and*

** the disposal by the target company or a subsidiary of the whole or a large part of its business or property.*

of the takeover scheme if the prescribed occurrence occurs in the final seven days. Yet an offeror may well be willing for a takeover scheme to proceed

notwithstanding, for example, that some new shares in the target company or in a subsidiary of the target company have been allotted. It is even conceivable that the offeror, the accepting shareholders and the target company itself may not realise for some time, or at all, that the takeover scheme had failed.

This problem does not arise with takeover announcements. With one exception,[41] s 684(1) provides that an on-market offeror may at any time until the close of the offer period withdraw unaccepted offers if a prescribed occurrence takes place.

The Legal Committee sees no reason in principle for this difference between offers and announcements. It proposes that an offeror under a takeover scheme have up to three business days after the end of the offer period to declare the offer to be free of a prescribed occurrence defeating condition. This three day period will allow the offeror sufficient time to consider all relevant events concerning prescribed occurrences up to the end of the offer period.

Proposal 26: Paragraph 663(2)(a) should be replaced with the following:
"(a) it is a term of the offer that the offeror may do so:
(i) in the case of a condition that a prescribed occurrence does not occur in relation to the target company, not more than three business days after the last day of the offer period; or
(ii) in any other case, not less than seven days before the last day of the offer period;
and the offer is declared to be free from the condition in accordance with that term;".
Paragraph 663(9)(b) should be replaced with the following:
(c) at the end of the offer period:
(i) the offers have not become free from the condition by the operation of subsection 664(2); and
(ii) the condition has not been fulfilled; and the offeror has not declared the offers to be free from the condition within the applicable period specified in subparagraph (2)(a)(i) or (2)(a)(ii).".

41. The offeror may not withdraw offers if the prescribed occurrence is one of the matters listed in paragraphs (a) to (g) of the definition of prescribed occurrence and the on-market offeror was entitled to more than 50% of the

voting shares in the target company at the time of the occurrence (paragraphs (a) to (g) cover matters that are within the control of the target company).

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Prohibitions on certain benefits: s 698

Subsections 698(2) and (4)

Subsections 698(2) and (4), which had no equivalent in CASA, prohibit the giving of discriminatory benefits where a takeover bid is proposed. In Magellan Petroleum Australia Limited v Sagasco Amadeus Pty Ltd[42], the Queensland Court of Appeal gave s 698(2) a wide interpretation which would prohibit an intending bidder from acquiring any shares in the proposed target company in the four months prior to the bid, except for acquisitions in the ordinary course of stock market trading (as permitted by s 698(5)). The Court acknowledged that its interpretation 'would prohibit the buying of shares off-market for cash during the four month period because the vendor would receive the benefit of immediate cash payment'. This seems an unintended consequence which serves only to fetter unduly an offeror's freedom to acquire on-market or otherwise up to a 20% entitlement in the target company before launching a takeover offer.

Subsections 698(2) and (4) also expose an associate of the proposing offeror to liability for breach even in circumstances where the associate is unaware of the proposing offeror's intentions.

These subsections are apparently designed to prevent an offeror from giving discriminatory benefits before the offer period beans and thereby circumventing the policy that equal opportunities be afforded to all shareholders. It should be kept in mind that because of the prohibition on escalation agreements (contained in s 697), a shareholder selling in advance of a takeover offer will not participate in any increased benefits provided under the takeover offer. Thus, it is not necessarily the case that an offeror, by paying a different consideration to a shareholder selling in advance of a takeover offer, discriminates in that shareholder's favour. The early sellers may do better or they may do worse. The important point is that shareholders the subject of the takeover offer itself all have an equal opportunity to participate in any benefits provided by the offeror. To the extent that it is appropriate to have regard to the price per share paid by the offeror for acquisitions made in advance of a takeover offer, the Legal Committee considers that s 641 and s 676 are adequate.

Proposal 27: Subsections 698(2) and (4) should be repealed.

Subsections 698(1) and (3)

The policy of s 698 is to prevent the giving of inducements to accept a takeover offer which are not equally available to all shareholders.

42. (1992) 10 ACLC 1,617. The High Court has granted leave to appeal; the matter has been set down for hearing on 16 March 1993.

As presently drafted, however, s 698(1) and (3) may be construed as prohibiting the giving of any benefits to an offeree, whether or not the benefits are intended to induce acceptance of its offers. In particular, the subsections may be construed as applying to payments made by the offeror in the ordinary course of its business.

Proposal 28: The Corporations Law should be amended to make it clear that s 698(1) and (3) apply only to benefits offered in connection with the acquisition or possible acquisition of a person's shares under the takeover scheme or announcement.

Subsection 698(5)

Paragraph 698(5)(b) provides that s 698 does not prohibit the acquisition of shares in a company in the ordinary course of stock market trading. The exception does not extend to on-market purchases of other securities of a target company. These purchases may constitute a 'benefit' to a shareholder who holds both shares and the other securities, for the purpose of the s 698 prohibition. The Legal Committee is of the view that purchases of other securities should be permitted provided the purchases take place through the stock market mechanism, to eliminate the possibility that the transaction is a particular inducement to accept the takeover offer.

Proposal 29: Paragraph 698(5)(b) should extend to securities of a company other than shares.

Names and addresses of shareholders: s 699

Section 699 enables an offeror to obtain a 'written statement' setting out, inter alia, the names and addresses of the shareholders in the target company. This provision does not enable the offeror to require the target company to provide address stickers or a computer disk with names and addresses even where they can be produced from the register of members. A hostile target company could thus put an offeror to the considerable and unnecessary expense of producing its own address stickers.

Proposal 30: Section 699 should be amended to enable an offeror to require the names and addresses of shareholders in the target company to be made available in a form, permitted by the technology of the target company, that is the most convenient for the offeror, provided that the offeror bears the reasonable cost of doing so.