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DISTRESSED DEALS: DOES AUSTRALIA'S TAKEOVERS PANEL HAVE A ROLE?

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Legal Briefings – By **Rodd Levy and Li-Lian Yeo**

As Covid-19 devastates sectors and firms, distressed deals have come to the fore. We size up the Takeovers Panel's role in deal disputes

The COVID-19 pandemic has had devastating impacts on the global economy, with many Australian companies, particularly in the tourism, retail and hospitality industries, falling into financial distress. Urgent corporate rescue deals inevitably need to thread the needle between the interests of competing stakeholders. This article considers the role of the Takeovers Panel in adjudicating disputes relating to companies in administration.

IN BRIEF
• An increasing number of companies are likely to fall into administration as government assistance programmes and temporary measures to protect directors from insolvent trading liability are wound back.
• While Courts remain the primary forum for resolving disputes in relation to an administration process, the Panel retains a limited role where the administration involves a Chapter 6 company.
• The Panel recently considered applications in relation to the conduct of the administration process in respect of *Virgin Australia*[1] and *Moreton Resources.*[2]

BACKGROUND

The effects of COVID-19 have been unprecedented, with governments having to balance the impact of regulatory action to control the spread of the virus (such as the imposition of lockdowns, border control and travel restrictions) against the direct impact those actions have on the economy.

Unsurprisingly, many companies, particularly in the tourism, retail and hospitality industries, have found themselves in financial distress. Not all will recover when current government assistance programmes are wound back.

In Australia, administrations governed by Part 5.3 of the *Corporations Act 2001* (Cth) (**Corporations Act**) are the process most commonly used for attempts to rescue and rehabilitate an insolvent company. In an administration, an administrator takes control of the company and its business with the objective of maximising the chances of the company or its business continuing to exist or, if this is not possible, to obtain a better return to the company's creditors and shareholders than would otherwise be the case in a winding up of the company.

In an administration, the future of the company is determined by a vote of creditors at the second creditors meeting, often by voting to accept or reject a proposed deed of company arrangement (**DOCA**).The voluntary administration process is focussed on providing a return to creditors, given the usual premise for the commencement of the process is that a company is insolvent or is likely to become insolvent. The Courts are the usual forum for resolving disputes relating to the conduct of the administrators who are themselves also subject to oversight and regulation by ASIC.

This article considers the role of the takeovers principles and the Takeovers Panel in relation to a Chapter 6 company that is in administration, including the Panel's recent decisions in relation to Virgin Australia and Moreton Resources.

THE PANEL'S LIMITED ROLE WHERE A COMPANY'S SHARES HAVE NO RESIDUAL VALUE

The takeover principles in the Corporations Act are directed at protecting shareholders and providing an efficient market for shares. Accordingly, where a company is in administration and its shareholders have lost all value in their shares, the takeover principles should have limited application.

The Panel accepted this position in *Pasminco*[3] where it found that the administrators' duties to conduct the affairs of an insolvent company to maximise the chances of the company and its business continuing in existence take precedence over Chapter 6 rights of shareholders.

While the Panel noted in *Pasminco* that its decision was not intended to be a watershed or tantamount to law reform, subsequent Panels have nonetheless adopted the principle that the Panel has a limited role to play where a company is in administration, particularly given the other more usual and appropriate forums for dispute that are available. For example, in *Kaefer,*[4] the Panel said at [7]:

The Panel's jurisdiction does not extend to regulating the affairs of companies in administration or conduct of company administrators under Part 5.3A. Any alleged impropriety in the conduct of a company administration is a matter for ASIC and/or the courts. Such an action may be brought by ASIC, in its discretion, or by disaffected shareholders or creditors.

The Panel has however made it clear that Chapter 6 considerations remain relevant and the Panel would not be prevented from conducting proceedings in relation to a company in administration, even if it may not do so often. Relevantly, in *Quantum,*[5] the Panel said at [14], as also referenced in *Virgin at* [39]:

> *We were mindful that the purposes of Chapter 6 may have limited relevance where a company is insolvent and no equity value remains in the shares. We were also concerned not to inappropriately obstruct action by the administrator to bring the company back to solvent operation. However, as was noted in Pasminco Ltd (Administrators Appointed), there is no exception from section 606 for deeds of company arrangement and calls for an exception were rejected by CASAC in its 1998 report. No change was made in that respect when Parliament "fine-tuned" Part 5.3A in 2007. It follows that the requirements of Chapter 6 must not be ignored.*

There are two limited scenarios where the Panel has previously heard matters regarding a company in administration:

- first, where the administration was a 'device' to allow parties to attain a goal relating to control through voting power without a bid, scheme of arrangement, substantial acquisition or other transaction involving shareholder participation;[7] and
- second, where the shares have or may have a positive value[6] (as in *Financial Resources Ltd* [2007] ATP 27 and *Quantum Graphite Ltd* (subject to deed of company arrangement) [2018] ATP 1).

VIRGIN AUSTRALIA AND MORETON RESOURCES

We set out below an overview of two recent matters brought before the Panel in relation to companies in administration.

VIRGIN AUSTRALIA

Virgin Australia entered into voluntary administration in April 2020. The highly publicised sales process for Virgin Australia culminated in Bain Capital emerging as the successful bidder and entering into a binding sale and implementation deed (**SID**) for the sale of the Virgin Australia group by an asset sale or, if approved by creditors, a DOCA.

A week after the SID was signed, two unsecured bondholders of Virgin Australia lodged a Panel application.

The bondholders had previously participated in the sales process and submitted an indicative proposal to the administrators. Relevantly they had entered into confidentiality agreements that in the usual way prevented them from contacting Virgin Australia stakeholders without the consent of the administrators.

The bondholders' principal allegation was that the sales process had been conducted in a way that was anti-competitive and designed to preclude an alternative DOCA emerging. In particular, the bondholders sought orders to:

- have their data room access reinstated;
- require that the administrators allow them access to Virgin Australia's stakeholders; and
- be provided with a copy of the SID (noting that the SID was relevantly subject to confidentiality orders made by the Federal Court).

After the bondholders submitted their Panel application, they also applied to the Federal Court for an order varying the SID confidentiality orders. The application was dismissed by the Court and shortly thereafter, the bondholders sought leave to withdraw their Panel application.

In determining to grant leave, the Panel made the following observations:

- first, safe-guards against lock-up devices for a solvent company are necessary to maximise value, though the Panel queried whether in the case of an insolvent company that is cash constrained, certainty of a transaction becomes more important.[8] In this regard, the Panel also considered the administrators' ASX announcement indicating that they did not expect there to be any value left in the shares;[9] and
- second, there was no public interest to obstruct or delay the administration process, particularly where there were other avenues available to the bondholders to pursue their ends (for example through the court process and by voting at the second creditors' meeting).

MORETON RESOURCES

Moreton entered into administration in June 2020, following which the administrators completed a sales process that resulted in the recommendation of a DOCA proposed by a former director of the company who was also a creditor (**Feitelson**).

Shortly after the recommendation was released in the creditors' report, the applicant who was also a former director of Moreton and a creditor, lodged a Panel application challenging various aspects of the administration.

The applicant made a number of allegations including in relation to deficiencies in the appointment of the administrators and inadequate disclosures in the report to creditors.

The Panel found in relation to those matters that other regulators or the Court are more appropriately placed to adjudicate.

The applicant also made separate submissions in relation to an alleged association between Feitelson and the other creditor which was dismissed by the Panel for a number of reasons including that the other creditor had not been consulted prior to the submission of the Feitelson DOCA and intended to vote against the DOCA.

After the initial Panel declined to conduct proceedings, the applicant applied to have that decision reviewed, which was also declined for a number of reasons, including that Moreton was in liquidation at the time the decision was made.

KEY TAKEAWAYS

Several themes emerge from the recent Panel cases:

- The court remains the primary and appropriate forum to adjudicate on disputes relating to administration processes.
- Takeover principle considerations remain relevant but may have limited application where there is no value left in the shares and there is no evidence of impropriety in relation to the administration process.
- In general, the administrators' assessment as to whether the company's shares have any residual value should be accepted in the absence of evidence to the contrary.
- The need for deal certainty where an insolvent company is cash constrained is a relevant public interest benefit that a Panel will take into consideration.

ENDNOTES

1. *Virgin Australia Holdings Limited (Administrators Appointed) 02* [2020] ATP 12.
2. *Moreton Resources Limited (Administrators Appointed) 02* [2020] ATP 14 and *Moreton Resources Limited (Administrators Appointed) 02 (Consent to review)* [2020] ATP 15.
3. *Pasminco Ltd (Administrators Appointed)* [2002] ATP 6.
4. *Kaefer Technologies Limited 02* [2004] ATP 16.
5. *Quantum Graphite Limited (subject to Deed of Company Arrangement)* [2018] ATP 1 at [14].
6. *Kaefer Technologies Limited 02* [2004] ATP 16 at [7].
7. For example in *Financial Resources Ltd* [2007] ATP 27 and *Quantum Graphite Ltd (subject to deed of company arrangement)* [2018] ATP 1.
8. *Virgin Australia Holdings Limited (Administrators Appointed) 02* [2020] ATP 12 at [43].
9. *Virgin Australia Holdings Limited (Administrators Appointed) 02* [2020] ATP 12 at [46].

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