ASIC'S CORPORATE FINANCE REPORT – JULY TO DECEMBER 2018: INSIGHTS AND GUIDANCE ON ASIC'S REGULATORY FOCUS FOR PUBLIC M&A

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Legal Briefings – By **Andrew Rich, Ken Ooi and Katerina Jovanovska**

We delve into the corporate finance report published in March by ASIC, with a focus on ASIC's public M&A related activities over the second half of 2018 and the future areas of ASIC's regulatory focus.

IN BRIEF

- Public M&A activity has increased, with 44 control transactions over the last six months of 2018 (compared to 29 in the previous six month period).
- ASIC's regulatory focus in the public M&A space has swung towards novel or complex consideration in schemes of arrangement, market and procedural integrity and corporate governance during takeovers.

ASIC'S CORPORATE FINANCE REPORT

ASIC has released its bi-annual report summarising its corporate regulatory activity over the second half of 2018.[1] This report contains key statistics and observations from ASIC's oversights of transactions over the period and offers forward looking insights into areas of focus.[2]

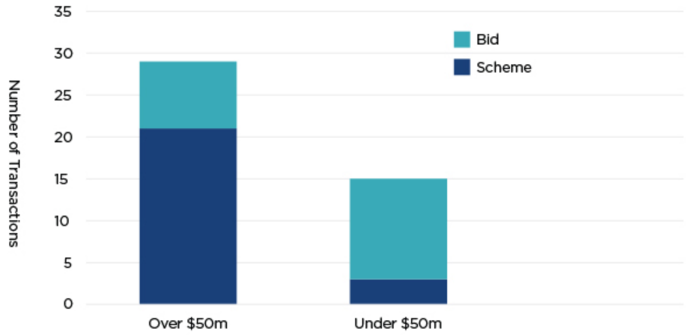
We provide some of the public M&A highlights below.

OVERVIEW OF PUBLIC M&A ACTIVITY

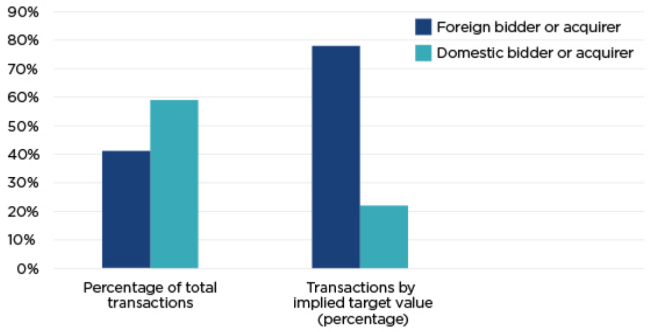
Public M&A activity over the period was high. ASIC reported 44 control transactions over the last 6 months of 2018, which represented an increase on the 29 in the previous 6 months.

Some observations worth noting from the period include:

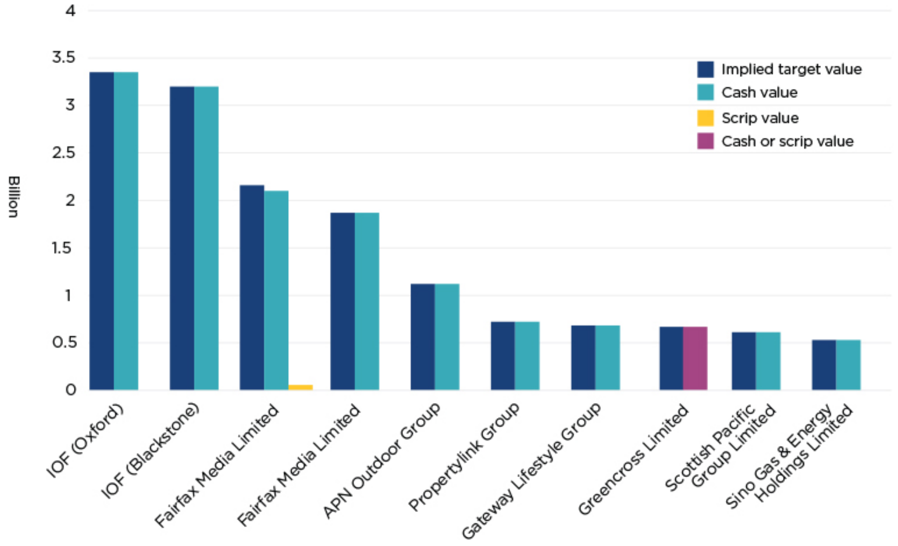
- **Schemes vs bids**: Consistent with the first half of 2018, although the number of control transactions undertaken by way of takeover and scheme were similar, the larger transactions were undertaken by way of scheme and the majority of the transactions under AU$50 million in value were undertaken by way of takeover. See Figure 1:



- **Continued offshore interest in Australia**: Offshore acquirers accounted for 78% by value and 41% by number of control transactions in the period. See Figure 2:



- **Cash remains king on big transactions**: Consistent with the first half of 2018, the largest control transactions were offers of all-cash consideration, with all-cash offers making up 8 of the top 10 offers. See Figure 3:



INSIGHTS FROM ASIC’S ACTIVITY AND FUTURE AREAS OF FOCUS

NOVEL OR COMPLEX CONSIDERATION IN SCHEMES

ASIC flagged its concerns about control transactions where the consideration offered is novel or complex.

Stub equity

In the recent Capilano Honey Limited scheme of arrangement (announced August 2018), shareholders were offered scrip consideration in the bid vehicle (an Australian proprietary company). ASIC argued in the Federal Court that it was contrary to the public policy underlying the provisions and legislative intent of the provisions governing proprietary companies to make a broad offer of scrip to more than 50 potential investors, with shares being held through a custodian arrangement to ensure the bid vehicle remains a proprietary company.

ASIC has reiterated its intention to issue a consultation paper on this topic. It has indicated that it may consider preventing control transactions announced that use this type of arrangement before the consultation ends.[3] See further our separate article on this topic.[4]

Consideration that is different between certain shareholders (fairness and equality)

ASIC provided a case study of a scheme involving a split consideration structure, under which shareholders were offered cash considerations for their first 20,000 shares and scrip for the balance of their holdings. This was the Mitula Group scheme of arrangement. ASIC has highlighted its concerns with potential unfairness between shareholders (with varying amounts of shareholdings) under this structure, as this creates the scenario where target holders are offered different considerations. ASIC has flagged that if different consideration structures between shareholders are proposed, the transaction will receive extra scrutiny.

Where such non-traditional approaches are proposed (where target holders are offered different consideration), which is not able to be addressed through usual measures, ASIC has suggested that it should be consulted before the scheme structure is finalised.

Schemes requiring a separate class

ASIC has reviewed a scheme where management employees were entitled to receive a combination of cash and scrip in the holding company of the bidder, while non-management shareholders were only offered cash consideration. ASIC's view was that this raised concerns about management and non-management shareholders voting in the same class despite their differing rights. Following ASIC's concerns, the scheme was amended to create a separate class for management shareholders.

MARKET AND PROCEDURAL INTEGRITY

ASIC has previously raised concerns about voting intention and other public statements.[5] It has re-emphasised its focus on ensuring that bidders and acquirers properly recognise the limits of agreements, arrangements and understandings reached with target holders.

CORPORATE GOVERNANCE DURING TAKEOVER TRANSACTIONS

ASIC has noted the important role that the target board plays in a takeover. ASIC has a close focus on governance and conflicts issues that may undermine the ability of the target board to carry out its duties and thereby impact the integrity of the takeover process. ASIC has provided examples of concepts such as ‘fiduciary outs’, which ASIC closely examines as well as adequate disclosure of directors benefits. More specifically, ASIC has said that bidders and targets should:

- not include an objective ‘reasonableness’ requirement on the target’s board in determining what are its fiduciary and statutory duties; and
- carefully consider any tailoring that may prevent the target board from relying on the exception when its duties may otherwise require.

See further our separate article on the topic of deal protections and fiduciary outs.[6]

CRIMINAL ACTIONS RELATING TO TAKEOVERS

ASIC has also reminded market participants that contraventions of the Corporations Act in relation to a control transaction can result in criminal prosecution and imprisonment. It provided a recent example of a current matter relating to an individual who knowingly made false or misleading statements to ASIC, that is being prosecuted by the Commonwealth Director of Public Prosecutions and is listed for a hearing on 15 July 2019.[7]

ENDNOTES

1. ASIC Report 612: ASIC regulation of corporate finance: July to December 2018.
2. ASIC’s data is based on disclosure documents lodged or otherwise released during the relevant period: See page 22 and 23 of ASIC Report 612.
3. ASIC, “18-376MR ASIC to consult on measures to restrict offers to retail investors of stub-equity in proprietary companies”, 13 December 2018.

4. Surveying the Stub Equity landscape post-Capilano.
5. ASIC Report 489: ASIC regulation of corporate finance: January to June 2016.
6. See Deal protection in the spotlight.
7. 18-336MR Man pleads guilty to misleading ASIC about shareholding.

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