

EVERYONE'S A WINNER: DAVID JONES' SCHEME IS APPROVED

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Legal Briefings - By **Rebecca Maslen-Stannage** and **Courtney Dixon**

SUMMARY

- Collateral benefits are not illegal in schemes of arrangement as they are in takeover bids.
- Schemes can accommodate different treatment of shareholders. Different treatment can go to class composition, whether votes should be tagged and whether the Court should exercise its discretion to approve the scheme.
- The best information for shareholders and the Court when asked to approve a scheme where someone may receive a benefit is an independent expert's report identifying the nature and extent of the benefit. However, clearly unusual factual circumstances may justify a departure from this standard.
- ASIC remains acutely focused on collateral benefit issues in relation to both bids and schemes.

RECENT EVENTS - SOLOMON LEW APPEARS ON DAVID JONES' REGISTER AFTER DISPATCH OF SCHEME BOOKLET, WOOLWORTHS ANNOUNCES CONDITIONAL TAKEOVER BID FOR COUNTRY ROAD

The Federal Court of Australia has approved the scheme of arrangement under which Woolworths (South Africa) would acquire David Jones (**Scheme**). Although the deal generated considerable media interest, it's worth quickly recapping on the relevant facts.

Shortly after release of the Scheme Booklet, David Jones' routine monitoring of its shareholder register outed prominent businessman, Mr Solomon Lew, as having acquired a small stake in David Jones. Mr Lew's presence was notable given his 17 year-long stalemate with Woolworths in relation to the strategic direction and management of Country Road (with Woolworths owning 87.88% and Mr Lew 11.8% of Country Road). Some weeks later, Mr Lew disclosed a holding of just below 10% in David Jones, if Mr Lew were to vote against the Scheme, its success would have been threatened.

Whilst the Scheme process was on foot – but before the Scheme meeting – Woolworths announced an off-market takeover bid for Country Road which was conditional on (among other things) the Scheme becoming effective.

The opportunity for Woolworths to acquire David Jones and the remainder of Country Road presented a potential 'win win' commercial outcome for Woolworths. Further, if the Scheme was approved, then David Jones shareholders would receive a premium for their shares, and a key condition to Woolworths' bid for Country Road – which provides Mr Lew with an exit from Country Road – would also be satisfied.

COULD WOOLWORTHS ACQUIRE DAVID JONES AS WELL AS THE MINORITY INTERESTS IN COUNTRY ROAD WITHOUT CONTRAVENING ANY TAKEOVER LAWS AND POLICIES?

Clearly, there were a variety of matters which required careful handling; however, there were some relevant principles in David Jones' favour to draw upon. For example, neither the equal opportunity principles in section 602(c) of the Corporations Act, nor the collateral benefit prohibition in section 623, apply directly to schemes. In a scheme context, issues of equal opportunity and collateral benefit are instead principally addressed through the voting processes (either in class composition or through the discounting or disregarding of votes) and adequacy of disclosure.

So – if under a scheme one shareholder is treated differently in terms of their legal rights, that may put them in a separate class. If they have some separate interest or benefit which is not under the terms of the scheme itself, the Court may take that into account in its fairness discretion whether to approve the scheme.

ASIC's view, from the outset, was that Woolworths' bid for Country Road was a benefit that was intended or likely to induce Mr Lew to vote in favour of the Scheme or to otherwise dispose of his David Jones shares, in circumstances where that benefit was not offered to other David Jones shareholders.

Where a scheme shareholder receives a collateral benefit in connection with a scheme, ASIC policy says that ASIC will generally not object to the scheme provided that the affected holder votes in a separate class or abstains from voting and the scheme booklet explains the benefit and includes an independent valuation of this benefit.

However, the fact pattern was unique in the David Jones deal and it was not possible for David Jones to follow this usual course. Mr Lew did not become a David Jones shareholder until after the dispatch of the Scheme Booklet (and therefore also after the first Court hearing). Usually, issues relating to collateral benefits arise at the time of negotiating the transaction and are therefore disclosed in the scheme booklet which is approved at the first Court hearing – not after.

On the information available to it, David Jones was not in a position to determine whether or not Mr Lew was in fact receiving a benefit, nor the scale of any such benefit, under Woolworths' bid for Country Road. Although David Jones had asked Mr Lew to abstain from voting on the Scheme, his intentions remained unknown until the Scheme meeting.

OBTAINING THE 'INFORMED CONSENT' OF DAVID JONES SHAREHOLDERS IN THE FACE OF UNUSUAL CIRCUMSTANCES

ASIC accepts that disinterested shareholders can approve 'collateral benefits' in the context of schemes. What information would be 'adequate' was the issue between ASIC and David Jones – and specifically whether an IER valuing 'the benefit' was essential.

David Jones faced unusual circumstances: David Jones, Country Road and Woolworths are all listed entities, and David Jones is both a competitor and customer of Country Road. David Jones did not have available to it (nor any immediate prospect of obtaining) the requisite confidential information and access to Country Road management, which were necessary to procure an IER.

David Jones was not hiding from the fact that there *could* be a benefit. But the feedback from its shareholders suggested that they did not care: they just wanted the opportunity to approve the Scheme and get their \$4.00 cash without further delay. Acting quickly and practically, David Jones prepared supplementary information to fairly disclose that there *may* be a benefit, including statements that:

- the lowest price at which Country Road shares traded in the 12 months prior to the Woolworths bid was \$3.33 and in the 3 months prior to the bid, \$9.80,
- media commentary suggested that \$17.00 was a generous bid price for Country Road,
- Country Road shares are extremely thinly traded and therefore share prices may not be a reliable guide to the fair value of its shares,
- David Jones shareholders might consider it unfair that Mr Lew has an offer for his Country Road shares which very substantially exceeds some recent trading prices and might exceed the fair value of Country Road shares, the timing of which appears to have been

affected by his acquisition of a stake in David Jones, and shareholders may consider this a reason to vote against the Scheme,

- if David Jones shareholders are concerned at the risk that Mr Lew will vote against the Scheme, shareholders may consider this a reason to vote in favour, to seek to maximise the chance of the Scheme vote being passed if Mr Lew votes against, and
- ASIC had queried whether the Country Road bid is a benefit that is intended or likely to induce Mr Lew to vote in favour of the Scheme or to dispose of his David Jones shares, in circumstances where that benefit is not offered to all David Jones shareholders.

The Court approved the dispatch of this supplementary disclosure, noting that *'while provision of an expert's report may be the best way to satisfy the Court ... it does not mean that it is the only way.'* But it is clear the Court is not holding this up as an example of best practice and will require unusual circumstances – such as existed in this deal – to allow it.

In approving the supplementary disclosure, the Court also noted that Country Road was required to procure an IER as to whether Woolworths' bid was fair and reasonable – this would include a valuation range of Country Road shares. On an aggressive timeline, this report would have been available in advance of the Scheme meeting or final Court hearing.

Ultimately the Court said that whether the supplementary disclosure is adequate would be a matter to be determined at the final Court hearing.

THE FINAL COURT HEARING – ASIC APPEARED BUT DIDN'T OPPOSE APPROVAL OF THE SCHEME

At the Scheme meeting, Mr Lew abstained from voting and the relevant approval thresholds were easily exceeded. These factors took the heat out of some arguments which were ventilated at Court. Although ASIC did not provide its usual section 411(17)(b) letter, it did not oppose the Scheme and pointed to that fact that Mr Lew had abstained from voting as a reason for this decision.

Her Honour, Farrell J, considered adjourning the final Court hearing until the Country Road IER was public so that the market and the Court were in a better position to assess any benefit which Mr Lew might receive through the Country Road bid. However, having regard to all the circumstances, including that any concerned David Jones shareholder could have sought an adjournment of the Scheme meeting to allow time to consider the Country Road IER (but none did so), her Honour decided, on balance, to approve the Scheme rather than to adjourn.

THE COURT'S ENDORSEMENT OF THE TAKEOVERS PANEL'S APPROACH ON COLLATERAL BENEFITS

It's worth mentioning one other point in her Honour's judgment which will provide welcome clarity to market practitioners – specifically, her Honour's endorsement, in a scheme context, of the Takeovers Panel's "net benefits" approach (in Guidance Note 21) as being the appropriate measure of whether a benefit exists.

KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.



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