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LONDON CALLING: COURT QUERIES WHETHER SCHEMES OF ARRANGEMENT CAN BE USED TO EFFECT TAKEOVERS

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Legal Briefings – By **Andrew Rich** and **Joshua Santilli**

In two recent decisions, the High Court of England and Wales has queried the legal basis for permitting the scheme of arrangement procedure to be used to effect change of control transactions. In this article, we consider these decisions and the implications for Australia.

IN BRIEF

- Change of control schemes are now a well-established and common feature of the commercial and regulatory landscape both in Australia and the UK.
- In two recent decisions of the High Court of England and Wales judges have queried whether (but ultimately accepted that) a change of control transaction can be characterised as an “arrangement” between a company and its members and therefore the subject of a scheme of arrangement.
- It is beyond doubt under Australian law that a change of control transaction is an “arrangement” between a company and its members and can therefore be effected by way of scheme of arrangement.

BACKGROUND TO CHANGE OF CONTROL SCHEMES

Schemes of arrangement which effect changes of control of widely held companies (**change of control schemes**) are, today, a well-established and common feature of the commercial and regulatory landscape in both Australia and the UK.

However, at various stages throughout the past century, challenges have been made to change of control schemes by dissentient members (and regulators) who have complained that the acquisition of companies by way of scheme of arrangement allows bidders to avoid the numerically higher 90% compulsory acquisition threshold that is required under a takeover bid (by way of contrast, a scheme of arrangement requires, among other things, a 75% vote).

In considering such challenges, courts have grappled with the question of whether a change of control transaction can properly be characterised as an "arrangement" between a company and its members and whether it is therefore able to be effected under the scheme of arrangement procedure. The requirement for an "arrangement" exists because schemes are a statutory creation, and the terms of the Australian and UK legislation require there to be an "arrangement" (or a "compromise") before the scheme of arrangement provisions can be engaged. Over time, courts have, rightly, accepted that a change of control transaction is an "arrangement".

NEW DOUBT

Although literally hundreds of change of control schemes have been approved by Australian and UK courts (and also by courts in other jurisdictions, including Singapore, Hong Kong and South Africa), two recent decisions of the High Court of England and Wales have (with respect, unnecessarily) queried the legal basis for change of control schemes.

The Jelf Group plc scheme

In the case of *Re Jelf Group plc* [2015] EWHC 3857 (Ch), which involved the acquisition of all the shares in Jelf Group plc by Marsh and McLennon Acquisition Limited (**MMAL**) by way of a change of control scheme, Justice Mann expressed some reservations to the proposition that a change of control transaction is an "arrangement". Notably, his Honour raised these reservations despite the absence of any opposition to the scheme of arrangement.

His Honour queried precisely what it was that made the proposed transaction an "arrangement" between Jelf Group and its members, noting that it simply provided for the sale of all the members' shares to the bidder, MMAL, and that Jelf Group's role in this purported "arrangement" was purely administrative (receiving consideration, possibly proposing amendments to the scheme and registering MMAL as the owner of the shares once transferred).

On that basis, Justice Mann opined that it might be stretching the concept of an "arrangement" to extend it to a change of control transaction (being, in his Honour's view, simply a "*contractual sale of shares to a purchaser in which the [target] company has what seem to be purely administrative functions*" rather than a true arrangement between the target company and its members).

His Honour went on to note that if he were considering the Court's jurisdiction to approve a change of control scheme "*entirely afresh and without the weight of history and authority"* he *"might well not have reached the decision that [the proposed scheme] was an 'arrangement' between the company and its members'*".

Despite that concerning prospect, his Honour correctly noted that "*it would not be right after all this time to undermine the clear understanding on which these transactions have taken place probably for decades*". Crucially, Justice Mann relied on previous authorities which held that a target company's obligation to register the scheme shares in the bidder's name was sufficient to make a change of control transaction an "arrangement" between the target company and its members.

Accordingly, his Honour proceeded to approve the Jelf Group scheme.

The SABMiller plc scheme

Justice Mann's comments in the *Jelf* decision were subsequently re-visited by Justice Snowden in the case of *Re SABMiller plc* – it appears that the issue was raised by Justice Snowden himself, rather than from the intervention of any dissenting shareholder.

The SABMiller transaction involved a proposal for a complex change of control transaction under which Anheuser-Busch InBev SA/NV (**AB InBev**), a Belgian company, would acquire SABMiller by way of a three-stage merger process, the first step of which was a UK change of control scheme.

In considering whether to approve the scheme Justice Snowden proceeded to re-ventilate the question raised in the *Jelf* decision as to why, if at all, a change of control scheme involved an "arrangement".

After considering submissions from counsel on the topic, his Honour ultimately concluded that, whilst there was an argument that a change of control transaction was not an "arrangement" for the purposes of the scheme of arrangement provisions in the UK Companies Act, there was a long history of schemes being used to facilitate takeovers and, although there might be doubts if the matter was considered afresh, it would not be right for the Court to differ from the weight of authority and the clear understanding of the position.

His Honour then approved the SABMiller scheme.

COMMENTARY

The discussions in the *Jelf* and *SABMiller* decisions are somewhat surprising given that they appear to raise doubts (albeit doubts that are subsequently dismissed in the judgments) which go to the very heart of the legal basis for a change of control scheme, namely whether it can be properly characterised as an "arrangement".

That the typical change of control scheme involves an "arrangement" for the purposes of the Australian and UK scheme of arrangements provisions should now be beyond all doubt (not that there was, in the view of the authors, any doubt before these two decisions).

Courts have, time and time again, interpreted the word "arrangement" (as it is used in the scheme of arrangement provisions) as a broad concept which can extend to a wide variety of corporate transactions, including those involving a change of control. The steady flow of scheme cases over many decades arriving at this same conclusion represents a tide that cannot (and should not) now be turned back.

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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