HERBERT SMITH FREEHILLS

REIMBURSEMENT OF TAKEOVER COSTS – SHOULD WE ADOPT THE NEW ZEALAND APPROACH?

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Legal Briefings – By **Rodd Levy and Zoe Leyland**

Abano Healthcare Group Ltd, a NZ listed healthcare investor and operator, recently obtained a New Zealand High Court ruling in its favour that it be reimbursed for all outstanding unpaid costs in relation to Healthcare Partners' failed hostile partial takeover offer.

IN BRIEF

- New Zealand provides a specific statutory mechanism for a target company to recover takeover response expenses from a bidder.
- In the Abano case, the New Zealand High Court departed from the previous distinction between expenses of a target in countering arguments in favour of a takeover (which were recoverable) and expenses directed at resisting a takeover bid (which were not recoverable).
- Abano established that, provided the expenses are not prohibited by the Takeover Code and they are properly incurred in relation to a takeover, they are recoverable.
- There is no statutory equivalent in Australia, meaning a target company wishing to recover its costs from a bidder would have to establish that there has been a breach of the legislative rules prohibiting misleading or deceptive conduct. This may prove difficult in practice.

BACKGROUND

In 2016, Healthcare Partners made a partial takeover offer for shares in Abano. At the time of making its offer, it held approximately 19% of the shares in Abano.

Healthcare Partners is owned by interests associated with its directors, one of whom was a former director of Abano.

Abano's board formed the view that the offer was not in the best interests of the company or its shareholders. In early 2017, the offer expired and Healthcare Partners had received acceptances for only 3.56% of the shares in Abano.

Shortly before the expiry, Abano announced it had "set-off" the dividend payable to Healthcare Partners given its non-payment of the expenses Abano incurred as a result of its failed takeover. Following the expiry, Abano sought to recover the balance through the courts.

New Zealand is unique in providing a specific statutory mechanism for a target company to recover expenses from a bidder. Specifically, Rule 49(2) of the Takeovers Code provided at the time for the recovery of, from the bidder, "expenses properly incurred by the target company in relation to … a takeover". This rule can be traced to a rule introduced into legislation in 1963. The provision has since been replaced by an equivalent provision in section 49 of the Takeovers Act, and the Takeovers Panel (rather than the Court) now has jurisdiction over such disputes.

WHAT COSTS ARE RECOVERABLE?

In reaching its decision, the Court departed from the principle established in 1972 in *Canterbury Frozen Meat Co Ltd v Waitaki Farmers' Freezing Co Ltd*. In that case, a distinction was drawn between expenses of a target in "countering arguments" in favour of a takeover and expenses directed at "resisting" a takeover bid. While the latter was not recoverable, the former was on the basis that it protected informed freedom of choice.

Given the current corporate environment is both more complex and regulated, the Court decided that the approach warranted fresh appraisal. Ultimately, the Court considered that actions to "resist" a takeover and those to "preserve" shareholder choice were often indistinguishable. Instead, the boundaries of properly incurred expenditure should be determined by reference to the Code, which prohibits defensive tactics (eg frustrating actions) and misleading or deceptive conduct.

On this basis, the Court ordered the failed bidder was liable to reimburse the target for costs incurred.

COULD SUCH COSTS BE RECOVERED IN AUSTRALIA?

Unlike in New Zealand, there is no express statutory right in Australia for a target company to recover its bid costs from a bidder. (However, there is a regime which gives target directors the right to recover, from the target, any expenses they reasonably incur in the interest of shareholders and in relation to the takeover bid.)

Accordingly, in Australia, any potential claim would have to rely on the target establishing that there had been a breach of a legislative rule prohibiting misleading statements and then relying on a statutory right of compensation.

That might arise, for example, if the bidder's statement was defective and the target incurred expenses seeking to have the bidder issue a corrective document. However, costs incurred in reviewing a compliant bidder's statement or issuing a target's statement would not be within the scope of that prohibition and could not be recovered.

In addition, even where there has been a defective bidder's statement or other document issued by the bidder, it may be difficult to claim compensation. The target would need to prove that a material amount of costs were incurred *as a result of* the offending conduct (such as defects in a bidder's statement), which may be hard where key advisers' fees are often fixed in quantum and therefore do not increase directly as a result of any such defects. Further, the bidder may be able to avail itself of a defence under section 670D if it was able (and willing) to prove that it did not know the bidder's statement was misleading or deceptive.

COMMENTARY: SHOULD A SIMILAR CONCEPT BE INTRODUCED IN AUSTRALIAN LAW?

Target companies often incur significant costs and expenses responding to a takeover bid. This can run to many millions of dollars. Is it fair that the bidder should be able to cause this with no responsibility?

The introduction of a right of recovery based on the New Zealand rule was considered in Australia in 1969, with the Company Law Advisory Committee chaired by Sir Richard Eggleston rejecting the concept on the basis that it was a normal cost of being in business and would suggest that the bidder "is in the wrong" in making a takeover bid.

On balance, while we are very sympathetic to the plight of target companies who are forced to incur significant expense dealing with defective takeover documents from a hostile bidder (and consider that an appropriate regime could be introduced for that situation), we tend to agree that the usual cost of responding to a takeover bid is better placed on the target rather than the party seeking to obtain control, who is generally required to offer a significant premium in order to do so. As the Company Law Advisory Committee also noted, complications would arise in the context of competing bids.

There is also the risk that introducing a general ability for a target to recover its costs could:

- create an administrative burden on the courts or the Takeovers Panel in assessing whether costs are properly incurred and in relation to the takeover bid; or
- lead to fewer takeover bids being made given bidder concerns in relation to being exposed to costs of an unknown quantum and outside its control, resulting in reduced competition in the market.

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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