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RESURGENCE IN ON-MARKET TAKEOVER BIDS

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Legal Briefings – By **Rodd Levy**

SUMMARY

- There has been an increase in on-market takeover bids recently.
- These bids may facilitate a very quick change of control and put a lot of pressure on the target and potential rival bidders.
- The different rules and features applicable to on-market bids can provide some tactical advantages for bidders.

RESURGENCE IN ON-MARKET TAKEOVER BIDS

There has been upsurge in the number of on-market takeover bids in recent times compared to previous experience.

There have been three on-market bids announced in the last 3 months. This compares to the yearly average of around 3.5 on-market bids per year over the previous 7 years.

But, before you get too excited, it is important to bear in mind that the vast majority of on-market bids have been fairly small in value.

In fact, since 2008, there have been 30 on-market bids, but only 6 exceeded $100m. The biggest by far was BG's successful $5.3 billion bid for Queensland Gas Company in 2008 and the next biggest was the $275m unsuccessful bid by Gujarat NRE Coking Coal for Jindal Steel & Power in 2013.

Excluding BG's bid as an outlier, the average value of these bids has been $54m. So we are talking about bids typically at the smaller end of the market.

Why can on-market takeover bids be attractive?

The main attraction of an on-market bid is its ability to facilitate a very fast change of control of the target company. This is because, as soon as the bid has been announced, the bidder is free immediately to start purchasing shares on the ASX in excess of the usual 20% limit.

This is the case even though the official offer period (which must be open for at least one month) only starts 14 days after the date of the announcement.

Great time pressure is placed on the target company directors. They only have 14 days from the date of the announcement to issue their target's statement, unlike in an off-market takeover bid where they are allowed 14 days after the official offer period starts (being the date when the bidder's statement is sent to target shareholders). So, effectively, there is half as much time to issue the response.

ASIC has power to extend the deadline for issuing the target's statement, but this is relatively rare, though it was granted recently to Phosphate Australia in the bid from Mercantile Investment Company (a bid with a value of about $3m).

Another key advantage for the bidder is, if the bidder later increases the offer price, it is not required to pay the higher price to shareholders that have sold early (unlike the position in an off-market bid where there is a statutory escalator). This rule arises as the shares are acquired on-market and there is no certain way of telling which shareholders have sold shares to the bidder. That can make an on-market bid cheaper for the bidder.

Conversely, shareholders may prefer the protections given by the statutory escalator in an off-market bid and, for this reason, be more inclined to accept such a bid earlier than they would an on-market bid. A bidder could therefore make an unconditional off-market bid in preference to an on-market bid. GRAM's current bid for PanAust (on which HSF is advising the target) is an example of an unconditional off-market bid.

Limitations of on-market bids

The main limitations of an on-market bid are that it must be unconditional and cash is the only consideration that can be offered.

For this reason, the bidder may be forced to take any or all shares put to it, even if that would not confer control. Therefore, on-market bids may cause issues for a bidder seeking to secure financing for the bid as lenders may be nervous that the bidder will not gain control and will not be able to control the cash flows and assets of the target company.

The unconditional nature of the offer will also mean that the bidder will not be able to protect itself from other events that are typically the subject of conditions in off-market bids, such as the target selling or buying a major asset.

The legislation gives some protection to bidders against formal ‘prescribed occurrences’ (such as new share issues and insolvency events). That rule will provide a basis for the Takeovers Panel’s rule against frustrating actions to apply, but the bidder is still left in a risky position compared to a bid with standard conditions.

We expect that on-market bids will remain infrequent, but they may be a suitable bid structure in the right cases.

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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