# Chapter 2

# Background

2.1 This chapter firstly provides an overview of the Takeovers Panel, its origins, role and functions. It concludes with a brief discussion of the issues raised by the *Glencore* decisions.

## The Takeovers Panel[1]

2.2 The Panel is the main forum for resolving disputes about a takeover bid until the bid period has ended. The Panel is a peer review body, with part time members appointed from the active members of Australia's takeovers and business communities.

2.3 The President of the Panel, Mr Simon McKeon, described to the committee the operations and composition of the Panel:

> ...in the seven years that we have been operating, our focus has been on providing a dispute resolution regime that is informal, expeditious and, most importantly, has the support of the market that we operate in. It is a peer review model. There are approximately 46 members of the Takeovers Panel, drawn from a wide variety of professions and businesses in this country and each appointed for the contribution that they can make to resolving takeover disputes in this country.[2]

2.4 At the public hearing, Treasury explained the takeovers arrangements prior to the commencement of the Panel:

> The panel's predecessor, the Corporations and Securities Panel, operated from 1991 to 1999 and made only four decisions during that time. Instead the courts were the primary focus for resolving takeover disputes, so parties to a takeover frequently engaged in tactical litigation to block bids. This caused delays and costs and prevented takeovers from occurring.[3]

2.5 Treasury explained that the Panel was modelled on the UK experience where takeover disputes:

> ...were resolved by a non-judicial specialist panel, which made prompt commercial decisions. This was seen as a very successful system. It

---

1 Parts of this summary are edited extracts taken from the Takeovers Panel's website, *About the Panel*, www.takeovers.gov.au (accessed 7 February 2007).

2 Mr Simon McKeon, President, Takeovers Panel, *Committee Hansard*, 1 December 2006, p. 6.

3 Ms Marian Kljakovic, Acting Manager, Market Integrity Unit, Corporations and Financial Services Division, Markets Group, Department of the Treasury, *Committee Hansard*, 1 December 2006, p. 23.

resolved disputes promptly and effectively and was copied in other common law jurisdictions.[4]

2.6 The Panel is established under section 171 of the *Australian Securities and Investments Commission Act 2001*. It is given various powers under Part 6.10 of the *Corporations Act 2001* (the Act). The Panel's primary power is to declare circumstances in relation to a takeover, or to the control of an Australian company, to be unacceptable. It has the power to make orders to protect the rights of persons (especially target company shareholders) during a takeover bid and to ensure that a takeover bid proceeds (as far as possible) in a way that it would have proceeded if the unacceptable circumstances had not occurred.

2.7 The policy principles that the Panel aims to advance are those set out in section 602 of the Act. They essentially include the four 'Eggleston Principles' and an additional principle that the acquisition of control of listed companies or listed managed investment schemes take place in an efficient, competitive and informed market.

2.8 Section 659AA of the Act describes the Panel as the 'main forum for resolving disputes' about takeover bids during the lifetime of those bids. Under section 659B, private parties to a takeover do not have the right to commence civil litigation, or seek injunctive relief from the courts in relation to a takeover, while the takeover is current. Disputes which were previously resolved in the civil jurisdiction of the courts will be resolved by the Panel. Like decisions made by other administrative bodies, Panel decisions are subject to judicial review by the courts.

2.9 The Panel also has various review powers. The Panel has the power to review certain decisions of the Australian Securities and Investments Commission (ASIC) to grant exemptions or modifications to takeovers parties from the application of various takeovers related provisions of the Act.[5] The Panel also has a function in reviewing its own, first instance, decisions.[6] In such circumstances the review Panel consists of a fresh group of Panel members. There can be only one review of an original decision. The Panel also has a review function if a matter is referred from the court.[7]

2.10 When a matter is referred, the Panel must consider whether it will commence proceedings. If it does, the substantive President of the Panel appoints three members

---

4 Ms Marian Kljakovic, Acting Manager, Market Integrity Unit, Corporations and Financial Services Division, Markets Group, Department of the Treasury, *Committee Hansard*, 1 December 2006, p. 23.

5 In certain circumstances section 655A allows ASIC to exempt a person from, or modify the application of, Chapter 6 provisions. Section 656A allows such decisions to be reviewed by the Panel. Similarly, section 656A allows the Panel to review decisions made by ASIC relating to its power to modify the substantial shareholding provisions under section 673 of the Act.

6 *Corporations Act 2001*, s. 657EA.

7 *Corporations Act 2001*, s. 657EB.

to be the 'sitting Panel'. If the substantive President is on any particular sitting Panel then he or she will be the sitting President. The substantive President and the selected Panel members must ensure that the selected Panel members do not have any material conflicts or biases.

2.11 The Panel is expressly required under the Australian Securities and Investments Commission Regulations 2001 to ensure that its proceedings are:

- as fair and reasonable;
- conducted with as little formality; and
- conducted in as timely a manner…[8]

2.12 The Panel has published Rules which govern its proceedings.[9] Evidence is gathered primarily in the form of written submissions although the sitting Panel may convene a conference. The Panel has significant powers at a conference, including the powers to take evidence on oath, subpoena witnesses, examine witnesses or subpoena documents.

2.13 Although the Panel is required to formally publish few documents it considers that the market and investors will be best served if its decisions and policies, and the reasons for its decisions, are published. The Panel publishes on its website:

- the text of any unacceptable circumstances declarations, and consequential orders, and decisions as well as the reasons for those decisions;
- any guiding policies and procedures; and
- any rules designed to clarify or supplement Chapter 6 of the Act or which govern Panel proceedings.[10]

## The *Glencore* decisions

2.14 The rationale for seeking amendments to the Act is two recent Federal Court decisions that considered the jurisdiction of the Takeovers Panel and the issue of equity derivatives.[11]

2.15 The facts surrounding the *Glencore* cases involved the takeover bid of Austral Coal (Austral) by the Centennial Coal Company (Centennial) in early 2005. At that time Glencore International AG (Glencore) had a 4.99 per cent stake in

8 Australian Securities and Investments Commission Regulations 2001, reg. 13.

9 These are made with respect to section 195 of the *Australian Securities and Investments Commission Act 2001*.

10 *Corporations Act 2001*, s. 658C and *Australian Securities and Investments Commission Act 2001*, s. 195, respectively.

11 *Glencore International AG v Takeovers Panel* [2005] FCA 1290 and *Glencore International AG v Takeovers Panel* [2006] FCA 274.

Austral. Glencore entered into 'cash settled equity swap' arrangements with two investment banks.[12] Under such arrangements the investor does not acquire any direct interest in any shares. The banks then bought shares in Austral (around seven per cent in total) to hedge their risk under the swap arrangements. Approximately two weeks after the combined holding had crossed the five per cent disclosure threshold Glencore announced to the ASX its holding and the existence of the swap arrangements.

2.16 In mid-2005, Centennial made an application to the Panel for a declaration of unacceptable circumstances in relation to Glencore's non-disclosure of its holding of Austral shares and the equity swaps. The non-disclosure was considered unacceptable by the Panel. This view was confirmed by a Review Panel, subsequently rejected by the Federal Court in the first *Glencore* case and later reconsidered for a third time by the Panel.

2.17 This time the Panel found that there was an 'effect' on the acquisition of a 'substantial interest' in the company.[13] The Panel considered that the swap arrangements, while they fell short of conferring a 'relevant interest',[14] nevertheless gave Glencore sufficient control over the relevant shares so that all the shares held by Glencore and the investments banks together constituted a 'substantial interest'. The Panel considered that Glencore had been able to benefit from this non-disclosure by acquiring shares for lower prices than if the true position had been disclosed. It ordered Glencore to make a payment of approximately 6.7 cents per share to Austral shareholders who had sold on market during the period of non-disclosure.

2.18 Glencore again contested the Panel's decision in the Federal Court. The court found that the Panel had erred in its decision that the non-disclosure of the cash settled equity swaps by Glencore was unacceptable.

---

12 A cash settled equity swap is an agreement whereby the investor (in this case Glencore) does not initially acquire an interest in any shares but essentially allows the investor to purchase the shares shortly after the swap is settled. It operates as an arrangement between an investor and a bank whereby the bank (for a fee) agrees to pay the investor an amount equal to the difference between the value of a given number of shares at the time of the closing out of the swap, and the value of those shares at the time when the arrangement was entered into. Under such an arrangement the investor does not acquire any interest in any shares. In order to hedge its risk under such an arrangement, a bank might buy the relevant shares. The agreement allows the swap to be settled which creates an incentive for the bank to minimise its exposure and divest its share holding. The investor would know this and be in an ideal position to acquire the shares at a price likely to be lower than the market price. Mr Lucas, Vice-Chairman, Financial Services Institute of Australasia, gave the committee a 'real-life' example of cash settled equity swaps, *Committee Hansard*, 1 December 2006, pp 19–20.

13 *Corporations Act 2001*, ss. 657A(2).

14 Section 608 sets out what a relevant interest in securities is. It states the basic rule of 'holding, or controlling voting or disposal of, securities'.

### *Relevant interest versus substantial interest*

2.19 The court decided that Glencore did not have a 'substantial interest', as required by subparagraph 657A(2)(a)(ii). In the court's view that expression requires a person to have an interest 'that can be a relevant interest or a positive power or right in relation to voting shares'.[15] The court said it would be a 'very curious result' if a person could be regarded as having a 'substantial interest' where neither the person nor any of their associates had any 'relevant interest' in any shares of the company. The court said that the scheme of the legislation was focused on regulating the acquisition of shares by reference to concepts of 'relevant interests' and 'voting power' and that the 'substantial interest' concept did not go broader than that.

2.20 The Law Council described two critical consequences of the interpretation of 'substantial interest' arising from the *Glencore* cases:

- first, that the Panel's jurisdiction to make declarations of unacceptable circumstances relating to the acquisition of a 'substantial interest' in a company or listed scheme is more limited than had been generally believed before this finding; and
- second, and of the greatest immediate policy concern, that the Panel now lacks the jurisdiction to regulate the disclosure of equity derivatives at the 5% level.[16]

### *The 'effect' test*

2.21 Section 657A(2)(a) currently states that, before it makes a declaration of unacceptable circumstances, the Panel must have regard to the 'effect' of those circumstances on the control of the company. The court was critical of the Panel's conclusion that the non-disclosure had had an 'effect' on Centennial's bid.[17] The Panel concluded that the non-disclosure affected Centennial's bid by making it successful sooner, to a greater extent and possibly at a lower price. However, the court found that the Panel had not explained these conclusions by reference to evidence before it. While the court accepted that, of necessity, the Panel must engage in some speculation, the Panel did not explain adequately how its conclusions about the effects of the non-disclosure were based, either on findings or inferences of fact.

---

15 *Glencore International AG v Takeovers Panel* [2006] FCA 274 at para 85.

16 Corporations Committee, Business Law Section, Law Council of Australia, *Submission 9*, p. 3.

17 As required by paragraph 657A(2)(a) of the *Corporations Act 2001*.