Australian Government

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Regards

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The Treasury

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The Secretary
Parliamentary Joint Committee on Corporations and Financial Services
Parliament House
PO Box 6100
CANBERRA ACT 2600

Dear Sir

INQUIRY INTO THE EXPOSURE DRAFT OF THE CORPORATIONS AMENDMENT (TAKEOVERS) BILL 2006

Thank you for the invitation to make a written submission to the inquiry.

On 7 September 2006, the Treasurer released an exposure draft of the Corporations Amendment (Takeovers) Bill 2006 (the Bill) and sought written comments on it. The terms of the exposure draft do not represent the concluded policy of the Government.

The reasons for the Bill are described in the attached document 'Corporations Amendment (Takeovers) Bill 2006 – Explanation'. Since March 2000, the Panel has generally succeeded well in its aim of acting as the primary forum to resolve disputes during takeover bid periods. In 2005-06, it received 33 applications. Its role has reduced tactical litigation substantially. The Government wants the Panel to continue to be able to perform that role effectively.

Five submissions were received in response to the release of the exposure draft of the Bill. They were lodged by the Law Council of Australia, Alan J Shaw Consulting, Australian Institute of Company Directors, the Financial Services Institute of Australia and Freehills. Copies are attached. The submissions were generally supportive of the Panel and of the aims of the Bill, but raised particular issues concerning the Bill.

This submission covers the principal points arising from submissions made to Treasury concerning the Bill.

Equity derivatives

We are aware that the *Glencore* cases highlighted issues regarding equity derivatives. The treatment of such derivatives is a significant question, which has recently exercised governments and panels internationally and was raised in some of the submissions. To address it would require extensive further consultation and perhaps significant adjustments to the *Corporations Act 2001*. This would delay the introduction of amendments to facilitate the Takeovers Panel carrying out the role for which it was designed.

Treasury is currently considering looking into the question of equity derivatives. It is, however, being treated as a separate issue. The current Bill has a narrower focus. Accordingly, it does not specifically deal with the issue of equity derivatives.

Definition of 'substantial interest'

The expression 'substantial interest' appears in three sections in the *Corporations Act 2001*, but is not currently defined in that Act. Subsections 602(b)(i) and (c) refer to acquiring substantial interests in a company, body or scheme. Subsection 657A(2)(a), and a related reference in subsection 657A(3), refer to acquiring a substantial interest in a company. Subsection 648G(5)(e) refers to proposals to acquire or increase the extent of a substantial interest in a company.

Sections 602 and 657A are two of the fundamental sections in Chapter 6 of the *Corporations Act 2001.* Section 602 is the first section of Chapter 6, setting out the purposes of the chapter. Section 657A gives the Panel the power to make declarations of unacceptable circumstances, and sets out when it has jurisdiction to do so.

The Explanatory Memorandum to the Corporate Law Economic Reform Bill 1998 might indicate that the expression was intended to have a wide meaning. It stated at paragraph 7.22:

> The Panel's jurisdiction to make a declaration of unacceptable circumstances will not depend upon the existence of a general offer to shareholders under a takeover bid. Instead, its discretion will extend to circumstances involving an acquisition of a substantial interest in, or control of, a company (Bill s 657A(2)(a)). In making a declaration of unacceptable circumstances, the Panel must have regard to the spirit of the takeover rules in section 602 in deciding whether the circumstances are unreasonable and whether it is in the public interest to make the declaration (Bill s 657A(2)).

In the *Glencore* cases, the expression 'substantial interest' was ruled to have a narrower meaning than had previously been considered to be the case. The intention of the Bill was to return to the position as it had been understood to be before the *Glencore* cases. The definition in the Bill states that a 'substantial interest' is not confined to particular matters, but does not attempt to define precisely what is encompassed by the term.

The approach taken in the exposure draft allows a flexibility which is consistent with the role of the Takeovers Panel and its case-by-case approach. A more comprehensive definition may result in problems when market practices change and would be inconsistent with a principles-based approach to drafting. It would probably be impossible to frame a completely comprehensive definition of 'substantial interest', even if that were considered desirable.

The Corporations Committee of the Business Law Section of the Law Council (the Council) suggested that the definition might 'cover interests in a company that do not concern rights relating to securities, such as those of employees, customers and suppliers'. We consider it unlikely the expression could be read in that way, given the context in which the term is used. Preliminary informal advice from the Australian Government Solicitor tends to confirm that view. We are, however, exploring this further. If the section is capable of such an interpretation, the wording could be adjusted to preclude that interpretation.

The Council's submission seems to indicate that, in their view, the provisions may be unconstitutional if the limits of the Takeover Panel's jurisdiction are too vague. It says:

> 'Legislative provisions which confer administrative powers in wide and ill-defined terms may be struck down as they allow a tribunal to define the limits of its own jurisdiction. While the High Court is likely to read down definitions and powers so that the powers of the panel do not exceed its constitutional limits, this is difficult to do when, as with the proposed definition of "substantial interest", the term is only defined in the negative.'

Preliminary advice from the Australian Government Solicitor is that there would not be a constitutional issue with the proposed wording in the Bill; the proposed provisions seem clearly to be within the corporations power.

The Council considers the definition is not needed at all, since the new subsection 657A(2)(b) would give the Panel power to deal with circumstances by reference to the policy objectives of section 602, and the Panel would not need to rely on subsection 657A(2)(a). For the reasons set out below, we consider that this is not necessarily a complete answer and that the current narrower interpretation of 'substantial interest' would still limit the operation of the new subsection 657A(2)(b).

If the Panel were to rely on the new subsection 657A(2)(b), it would need to consider the effect of circumstances, having regard to the purposes set out in section 602. Subsections 602(b) and (c) still define those purposes by reference to the acquisition of substantial interests. So if the restricted interpretation of 'substantial interest' is allowed to remain, it would mean subsections 602(b) and (c), and subsection 657A(2) operating through them, would still not apply where there is no acquisition of a substantial interest in that restricted sense. Nor would there necessarily be an acquisition of control over voting shares, sufficient to bring subsection 602(a) into play. If 'substantial interest' retains its restricted meaning, there could be situations in which the spirit of the law was being contravened, but the circumstances did not fall within the wording of section 602. Arguably, the more specific provisions in subsections 602(b) and (c) might also lead to a narrower view being taken when applying subsection 602(a).

Wording of the proposed s.657A(2)(b)

The wording of the proposed new subsection would allow the Panel to intervene if circumstances:

> are otherwise unacceptable (whether in relation to the effect that the Panel is satisfied the circumstances have had, are having, will have or are likely to have in relation to the company or another company or in relation to securities of the company or another company) having regard to the purposes of this Chapter set out in section 602

The Council suggested replacing 'having regard to' with 'because they are inconsistent with or contrary to'. If we have understood the Council correctly, the aim is to ensure the wording is 'more firmly linked to established policy and public interest requirements to avoid new jurisdictional issues'. The Australian Institute of Company Directors was also concerned the proposed wording might be vulnerable to constitutional challenge on the basis that it was an attempt to give the Panel power to define its own jurisdiction. We are taking advice on this point but do not at present consider it is likely to be a significant risk.

We consider the change proposed could result in unduly narrowing the Panel's ability to act.

Should the Parliamentary Joint Committee require further information on the issues raised by the exposure draft or this submission, we are very willing to provide it.

Yours sincerely

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