HANDING THE CORPORATE REINS TO CREDITORS: THE ROLE OF THE TAKEOVERS PANEL IN THE PASMINCO ADMINISTRATION

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I INTRODUCTION

The Takeovers Panel ('the Panel') has played an increasingly important role in Australian corporate regulation since it was given expanded powers in March 2000, when the *Corporate Law Economic Reform Program Act 1999* (Cth) ('*CLERP Act*') was enacted. These last few years have been a significant period for the revitalised Panel. The Panel has successfully established itself and built market confidence in its new role of replacing the courts in resolving takeover disputes. Notwithstanding its focus on takeovers, the Panel has decided a wide variety of issues in the 70 decisions since the *CLERP Act* commenced.[1]

This article examines the Panel's decision in *Re Pasminco Ltd (admin apptd)*[2] ('*Pasminco*'). The case is a significant decision in the history of the new Panel.[3]

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1 As at 15 November 2002. Prior to the reforms, the Panel had delivered only four decisions since it was established as the Corporations and Securities Panel by the *Australian Securities Commission Act 1989* (Cth) s 171. Its first members were appointed in 1991: Michael Duffy, Attorney-General, 'Appointments to the Corporations and Securities Panel' (Press Release, 2 July 1991). On the early Panel, see Emma Armson, 'AAT Review of the ASC's Decision to Apply or Not to Apply to the Corporations and Securities Panel' (1994) 12 *Company and Securities Law Journal* 439; Nicole Calleja, 'Furthering the Objectives of the Corporations Law Takeover Provisions: Will Simplification Help?' (1997) 15 *Company and Securities Law Journal* 208; Michael Gething and Kimberley Ould, 'The Westfi Takeovers Panel Application: Lessons for the Future' (2000) 18 *Company and Securities Law Journal* 351; John M Green, 'An Australian Takeover Panel — What Do We Want? A Panel Poll and Critique' (1989) 7 *Company and Securities Law Journal* 6; John M Green and Stephen Brent, 'Takeovers: Breathing More Life into the Corporations and Securities Panel' (1997) 15 *Company and Securities Law Journal* 319; Barbara Mescher, 'Regulation of Takeovers by the Corporations and Securities Panel: The Occurrence of Unacceptable Circumstances' (1994) 4 *Australian Journal of Corporate Law* 90; G F K Santow and George Williams, 'Taking the Legalism Out of Takeovers' (1997) 71 *Australian Law Journal* 749; George Williams, 'The Corporations and Securities Panel: What Future?' (1994) 12 *Company and Securities Law Journal* 164.

2 (2002) 41 ACSR 511. The Panel comprised Denis Byrne (sitting President), Marian Micalizzi (sitting Deputy President) and Irene Lee.

It deals with fundamental and novel questions about the rights of shareholders and creditors, and the tension between them that arises where a company is insolvent. These issues are dealt with in the context of determining whether creditors should be exempted from the protections provided to shareholders under the takeover provisions. The case illustrates the wide-ranging impact that the Panel's decisions can have upon corporate law, even though the Panel's new role was chiefly designed to avoid tactical litigation by cutting through the complexities of takeover matters and making efficient decisions with a commercial focus.

The decision is also noteworthy as it is the first Panel matter to include a dissenting opinion.[4] This highlights the difficult nature of the issues raised in the case. It also raises the prospect of the Panel looking more like a court. One of the features of the new regime was that the Panel would resolve takeover disputes 'as quickly and efficiently as possible'[5] in place of a more rigid court process.[6] Anticipating concerns that different opinions may undermine this, the press release accompanying the decision emphasised that 'the process of settling majority and dissenting reasons had not materially affected the timing of making and releasing the decision'.[7]

The *Pasminco* case involved a company that could not pay the approximately A$2.9 billion that it owed to creditors.[8] As a result, the company was placed under administration. The administrators proposed a scheme to allow the creditors to minimise their losses by continuing to conduct Pasminco's business. Rather than creating a new company, the proposal was to issue a large number of shares in the existing company (referred to as 'the company shell'). The shares would be issued under a deed of company arrangement, through which the creditors would largely agree to forgive the debts the company owed to them.

Ultimately, the plan was to revive the company so that its listing on the Australian Stock Exchange Limited ('ASX') could be restored. As the ASX required a minimum number of shareholders for listing, it was proposed to rely upon the number of shareholders in the company prior to the administration (referred to as 'the shareholder spread').

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3 On the post-*CLERP Act* Panel, see Nicole Calleja, *The New Takeovers Panel — A Better Way?* (2002); Michael Hoyle, 'Some Observations on the Takeovers Panel' (2002) 20 *Company and Securities Law Journal* 183; Jennifer Hill, 'Back to the Future? Bigshop 2 and Defensive Tactics in Takeovers' (2002) 20 *Company and Securities Law Journal* 126; Barbara Mescher, 'Powers of the Takeovers Panel and their Effect upon ASIC and the Court' (2002) 76 *Australian Law Journal* 119; Emmanuel Hadjidakis, 'The Takeovers Panel: From Toothless Tiger to Sleeping Tiger? Will the Courts Now Advance?' (2002) 20 *Company and Securities Law Journal* 59; Rodd Levy, 'Pinnacle 8: New Duties for Target Directors' (2001) 19 *Company and Securities Law Journal* 329.

4 The dissenting reasons were given by Micalizzi DP.

5 See Corporate Law Economic Reform Program, *Takeovers Proposals for Reform* Paper No 4 (1997) 36; Explanatory Memorandum, Corporate Law Economic Reform Program Bill 1998 (Cth) 38.

6 Corporate Law Economic Reform Program, above n 5, 34–6 and Explanatory Memorandum, Corporate Law Economic Reform Program Bill 1998 (Cth) 38.

7 Takeovers Panel, 'Panel Publishes Decision and Reasons in Pasminco' (Press Release TP02/23, 26 April 2002).

8 See Pasminco Australia, *Investor Information* (2002) <http://www.pasminco.com.au/index.asp?link_id=2> at 5 October 2002.

Two key issues arose in the *Pasminco* case. First, the Panel considered whether the company shell and shareholder spread could be used for the benefit of creditors, without the approval of the existing shareholders ('pre-administration shareholders'). This generates some novel issues. In particular, it raises the question whether the pre-administration shareholders had any interest in the company apart from their shares and, in particular, any interest in the shareholder spread that they generated in the company.

Second, the issue of the shares to the creditors involved agreements that would breach the takeover provisions.[9] Unlike the alternative methods of achieving the administrators' aims, there is no specific takeover exception in the *Corporations Act 2001* (Cth) ('*Corporations Act*') for acquisitions under a deed of company arrangement. Consequently, the Panel had to consider whether the takeover powers of the Australian Securities and Investments Commission ('ASIC') should be used to exempt the creditors in this case. The majority decided to grant this innovative relief.

This article is divided into five parts. Part II provides a detailed account of the facts in the case and its outcome. Part III analyses the general company law principles underlying the decision to allow the creditors to use the company shell and shareholder spread. Part IV examines the takeover policy issues generated by the majority's decision to grant the takeover relief. Part V concludes that the outcome of the case was justified and discusses what can be learnt about the Panel from this decision and the issues raised.

II THE *PASMINCO* CASE

The directors of Pasminco Limited ('Pasminco'), a large Australian mining company, appointed voluntary administrators ('the administrators') to Pasminco and its wholly-owned Australian subsidiaries on 19 September 2001.[10] This required the directors to form the opinion that the company was 'insolvent' or 'likely to become insolvent at some future time'.[11] In their statement to the ASX on the same day, the directors stated that they 'were unable to form a view that there were reasonable grounds to believe that the Company could meet all of its commitments as and when they fall due'.[12] Trading in Pasminco shares on the ASX was suspended following the directors' announcement.[13]

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9 *Corporations Act 2001* (Cth) s 606.

10 However, Pasminco Superannuation Pty Limited did not have voluntary administrators appointed: see *Pasminco Limited (Subject to Deed of Company Arrangement) Annual Report 2002* (2002) 1, <http://www.pasminco.com.au/index.asp?link_id=8.1046> at 13 November 2002.

11 *Corporations Act 2001* (Cth) s 436A(1). Under *Corporations Act 2001* (Cth) s 95A, a person is insolvent if they cannot pay their debts as and when they become due and payable.

12 Pasminco Ltd, 'Appoints Voluntary Administrators' (Announcement to ASX, 19 September 2001), <http://www.asx.com.au/asx/statistics/AnnDetail.jsp?id=426489&&issuerid=975 > at 5 October 2002.

13 Australian Stock Exchange, 'Suspension from Official Quotation' (ASX Market Release, 20 September 2001), <http://www.asx.com.au/asx/statistics/AnnDetail.jsp?id=426518&&issuerid=975> at 5 October 2002.

Appointing the administrators compounded the company's parlous financial situation because it triggered significant financial obligations owed to a number of banks.[14] The *Pasminco* case was ultimately brought to the Panel for the benefit of the six banks that were the Pasminco Group's principal financiers and creditors.[15] In summary, the administrators concluded that Pasminco:

- had liabilities that materially exceeded its assets;
- needed the creditors' support to pay its debts (the administrators had this support, which the directors had been unable to attain); and
- could be liquidated by the creditors, with no payment to shareholders.[16]

The administrators considered a deed of company arrangement to be a better outcome for creditors than liquidation. They advised that liquidation may have resulted in a worse position for creditors than it would have for shareholders.[17] In contrast, a deed of company arrangement potentially allowed the creditors to minimise their losses by trading the company out of difficulty (and out of the period of very low base metal prices).[18] Instead of transferring Pasminco's assets to another company, it was proposed that the administrators retain use of Pasminco as a corporate entity (the company shell) and, in time, Pasminco shares be traded again on the ASX with the benefit of the number of pre-administration shareholders (shareholder spread) to satisfy the liquidity requirements in the ASX Listing Rules.[19]

This proposal provided an obvious benefit to the creditors, as it avoided the need to create a new entity and transfer Pasminco's assets into it. However, it appears that the administrators did not put forward a detailed argument to the Panel on this issue. At one point, the administrators advised that they were only speculating as to the possible advantages of the proposal to acquire control of the corporate entity.[20] However, the administrators did submit that there were no taxation or other advantages in using the existing company rather than a different corporate entity.[21]

Under the proposed reconstruction, a large number of Pasminco shares would be issued to the creditors under a deed of company arrangement. The administrators advised that this would likely result in the creditors holding 95–99 per cent of Pasminco's shares, with the remaining shares to be held by the pre-administration shareholders.[22] This conversion of the creditors' debt into equity

14 *Pasminco* (2002) 41 ACSR 511, 517–18 (Byrne P and Lee).

15 Ibid 543–4.

16 Ibid 513 (Byrne P and Lee), 535 (Micalizzi DP).

17 Ibid 513–14 (Byrne P and Lee).

18 Ibid 517 (Byrne P and Lee).

19 Australian Stock Exchange Listing Rule 1.1. Condition 7 requires a minimum of 500 shareholders, each holding ordinary shares worth at least A$2000.

20 *Pasminco* (2002) 41 ACSR 511, 522 (Byrne P and Lee), 539 (Micalizzi DP).

21 Ibid 522 (Byrne P and Lee).

22 Ibid 519 (Byrne P and Lee). See also Pasminco Ltd, 'Outcome of Takeovers Panel Proceedings' (Announcement to ASX, 30 April 2002), <http://www.asx.com.au/asx/statistics/AnnDetail.jsp?id=480304&&issuerid=975> at 5 October 2002.

reflected the risk that they would be taking in continuing the company's operations.[23]

The proposed share issue to creditors would involve a breach of the takeover prohibition in s 606 of the *Corporations Act*.[24] No individual creditor would acquire shares with more than 20 per cent voting power.[25] Rather, the proposal would require the creditors to enter into agreements that would breach the takeover provisions as they would control the disposal of shares during the restructure.[26] The agreements also related to the control of Pasminco and the conduct of its affairs.[27] These agreements would result in an increase in voting power[28] through the definitions of 'relevant interest'[29] and 'associate'[30] respectively.

Unlike the provisions in relation to the alternative procedures available to the administrators,[31] there is no specific legislative exception from the takeover provisions for shares acquired under a deed of company arrangement. On 14 December 2001, the administrators applied to ASIC for a takeover exemption for the acquisitions under the proposed deed of company arrangement.[32] ASIC refused the application on 4 February 2002.[33]

Pasminco applied to the Panel for review of ASIC's decision on 19 February 2002.[34] The *CLERP Act* gave the Panel the power previously held by the Administrative Appeals Tribunal to review certain takeover decisions made by ASIC.[35] The rationale for this included enhancing the Panel's ability to provide guidance to ASIC on takeover issues when exercising the Panel's general jurisdiction to deal with unacceptable circumstances.[36] Another reason would likely have been to promote consistency in administrative decision-making in the takeover context.

A majority of the Panel reversed ASIC's decision on 22 April 2002.[37] The majority decided that the creditors should be exempted from the takeover provisions, and that the company shell and shareholder spread should be able to be used for the benefit of the creditors. The dissenting Panel member came to the opposite conclusion on both issues.

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23 *Pasminco* (2002) 41 ACSR 511, 535 (Micalizzi DP).

24 *Corporations Act 2001* (Cth) s 606 prohibits acquisitions that increase a person's voting power from 20 per cent or below to above 20 per cent in issued voting shares of a listed company or unlisted company with more than 50 members.

25 *Pasminco* (2002) 41 ACSR 511, 520 (Byrne P and Lee).

26 Ibid 520. The restructure was estimated to take between one and 10 years.

27 Ibid 520 (Byrne P and Lee).

28 *Corporations Act 2001* (Cth) s 610.

29 *Corporations Act 2001* (Cth) s 608(1)(c).

30 *Corporations Act 2001* (Cth) s 12(2)(c).

31 Discussed in detail in Part IV below.

32 *Corporations Act 2001* (Cth) s 655A; *Pasminco* (2002) 41 ACSR 511, 544.

33 *Pasminco* (2002) 41 ACSR 511, 544.

34 *Corporations Act 2001* (Cth) s 656A; *Pasminco* (2002) 41 ACSR 511, 544.

35 This includes the power to review ASIC decisions on whether to exempt persons from the takeover provisions in ch 6 of the *Corporations Act 2001* (Cth), or to modify the application of ch 6 to them: *Corporations Act 2001* (Cth) s 656A(1)(a).

36 See *Corporations Act 2001* (Cth) s 657A.

37 *Pasminco* (2002) 41 ACSR 511, 544.

As the creditors had not yet met to consider or vote on a deed of company arrangement, the majority granted the exemption on the basis that certain events would take place. The exemption applies to each creditor, who is bound by a deed of company arrangement that is materially consistent with the application to the Panel, for acquisitions of Pasminco shares under the deed.[38] This approach is efficient from a regulatory perspective, as it avoids the need for the Panel to supervise the Pasminco administration.[39]

The takeover exemption was granted subject to conditions requiring specific disclosure to shareholders and the market.[40] Although the dissenting Panel member disagreed with the decision to grant the exemption, they supported the disclosure requirements set out in the conditions.[41] The conditions were designed to remedy the lack of information available, particularly for Pasminco's shareholders and directors. They required Pasminco to provide, through an ASX announcement, Pasminco's website and national and State newspapers,[42] adequate disclosure on:[43]

(1) the exemption within two business days — including that the existing shares would be heavily diluted but not cancelled (to rectify a misconception amongst some of the shareholders)[44] and the possible timeframe for future events; and
(2) the proposal, when the administrators had a firm proposal to put to creditors — including:
    (a) that assets would be applied in the first instance in creditors' interests;
    (b) any potential share value that the administrators saw for shareholders;
    (c) a further announcement that the existing shares would be heavily diluted but not cancelled; and
    (d) details of the restrictions on creditors selling shares under the restructure.

III USE OF CORPORATE ENTITY AND SHAREHOLDER SPREAD

A To Whom Does the Corporate Entity and Shareholder Spread Belong?

A key issue for the Panel was whether the corporate entity of Pasminco (company shell) and the number of pre-administration shareholders (shareholder spread) could be used for the benefit of creditors without the approval of those

38 Ibid.
39 Ibid 532 (Byrne P and Lee), 535 (Micalizzi DP).
40 Ibid 544.
41 Ibid 535 (Micalizzi DP).
42 Ibid 531 (Byrne P and Lee). Shareholders would also need to be advised that they could obtain a copy of these notices without charge.
43 Ibid 544.
44 Ibid 527–8 (Byrne P and Lee).

shareholders. The majority and minority came to opposite conclusions on this issue. It is implied in the majority view that the concept of a separate 'listed shell' to which the shareholders retain a residual value is misleading. The majority considered that the 'listed shell of Pasminco' is 'just the company Pasminco Limited, to which the administrators have been appointed'.[45] Similarly, they stated that '[t]he company's listed status is a contractual relation between the company and ASX. It is not a separate entity or item of property, which must be notionally hived off and dealt with separately'.[46]

The majority consequently concluded that both the corporate entity and shareholder spread are assets that could be used by the administrators 'primarily' for the benefit of creditors.[47] In contrast, the minority considered that the creditors did not have the right to access the shareholder spread and listed shell[48] of Pasminco as they are assets of the original shareholders.[49] In particular, the minority argued that, although the creditors have the power to destroy any value remaining in these assets by placing the company into liquidation, this does not give the creditors the right to use these assets for their benefit.[50] Neither the majority nor minority discussed the principles underlying these issues in any significant detail.

1 *Corporate Entity*

A company's separate personality is a fundamental tenet of company law. It is clear from the authorities that the company has a distinct legal existence from its shareholders.[51] The separate concept of limited liability means that shareholders are only required to contribute any amounts that they have not yet paid for their shares.[52] When combined, these principles provide a generally effective barrier between a company's creditors and its shareholders. Subject to certain legislative and common law exceptions,[53] the creditors will only be able to look to the company's resources for payment.[54]

Shareholder rights are determined by the *Corporations Act*,[55] the company's constitution and the common law. For the purposes of this discussion, the shareholders' rights have been divided into the main categories of voting rights and economic rights, the latter being the payment of any dividend and any

45 Ibid 530 (Byrne P and Lee).
46 Ibid.
47 Ibid.
48 Ibid 534 (Micalizzi DP). This term refers to both the corporate entity and the fact that it is listed on the ASX.
49 Ibid.
50 Ibid 535 (Micalizzi DP).
51 *Salomon v Salomon & Co* [1897] AC 22; *Industrial Equity Ltd v Blackburn* (1977) 137 CLR 567.
52 *Corporations Act 2001* (Cth) s 9, 'company limited by shares'.
53 See, eg, the insolvent trading provisions in *Corporations Act 2001* (Cth) ss 588G, 588V and the common law on piercing the corporate veil (such as *DHN Food Distributors Ltd v Tower Hamlets LBC* [1976] 1 WLR 852; *Briggs v James Hardie & Co Pty Ltd* (1989) 7 ACLC 841).
54 *Salomon v Salomon & Co* [1897] AC 22; *Industrial Equity Ltd v Blackburn* (1977) 137 CLR 567.
55 Assuming that the company has been incorporated under the *Corporations Act 2001* (Cth) or previous corresponding legislation (as in this case).

surplus on winding up. After a company is placed in administration, it is the creditors (not the shareholders) who are given voting rights to determine the future of the company.[56] This is consistent with the principle that directors have a duty to take into account the interests of creditors where a company is insolvent or nearing insolvency, although it is not an obligation that creditors can enforce directly.[57]

The economic rights of shareholders in an insolvency situation will depend upon whether there are sufficient assets in the company to repay creditors. Assuming that the administrators assessed correctly that Pasminco was insolvent without the support of its creditors, the shareholders could not expect a return of their capital in a winding up.[58] Even the minority agreed that 'the shareholders have always been exposed to getting nothing of value for their Pasminco shares, under this or any alternative proposals'.[59]

However, the minority was concerned whether the valuations relied upon to assert there was no value left for shareholders were for fair value and whether they properly took into account the assets' prospects and related risks.[60] The concern that the valuation was based upon '"fire" sale asset prices', in this case because base metal prices were at a 'historic low',[61] is one that can often arise in an insolvency context. In the analogous situation of a receiver selling assets to pay for the debts of higher ranking secured creditors, the *Corporations Act* places a duty on the receiver to sell an asset either at not less than its market value or, if it does not have one, at 'the best price that is reasonably obtainable, having regard to the circumstances existing when the property is sold'.[62] This is consistent with the administrator being able to value the assets at their prevailing market value, without taking into account any future value that may be attributable to future movements in metal prices[63] or the administration.

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56 See *Corporations Act 2001* (Cth) ss 436E, 439A–C and Justice Robert Austin and Robert Brown, 'Voluntary Administrators as Fiduciaries' in Ian Ramsay (ed), *Key Developments in Corporate Law and Trust Law* (2002) 179, 196.

57 *Geneva Finance Ltd v Resource & Industry Ltd* (2002) 20 ACLC 1427; *Spies v R* (2000) 201 CLR 602, 635–7 (Gaudron, McHugh, Gummow and Hayne JJ); *Re New World Alliance Pty Limited; Syncotex Pty Ltd v Baseler (No 2)* (1994) 51 FCR 425, 444–5 (Gummow J); *Kinsela v Russell Kinsela Pty Ltd (in liq)* (1986) 4 NSWLR 722, 729–33 (Street CJ, with whom Hope and McHugh JJA agreed). See generally Austin and Brown, above n 56, 196; J D Heydon, 'Directors' Duties and the Company's Interests' in P D Finn (ed), *Equity and Commercial Relationships* (1987) 120, 123–4, 126–36; I A Renard, 'Commentary' in P D Finn (ed), *Equity and Commercial Relationships* (1987) 137, 140; Jennifer Hill, 'Public Beginnings, Private Ends — Should Corporate Law Privilege the Interests of Shareholders?' in Fiona MacMillan (ed), *International Corporate Law* (2000) vol 1, 17, 24–6; Andrew Keay, 'The Director's Duty to Take into Account the Interests of Company Creditors: When is it Triggered?' (2001) 25 *Melbourne University Law Review* 315; James McConvill, 'Directors' Duties to Creditors in Australia after *Spies v The Queen*' (2002) 20 *Company and Securities Law Journal* 4.

58 *Pasminco* (2002) 41 ACSR 511, 513 (Byrne P and Lee), 535 (Micalizzi DP).

59 Ibid 535 (Micalizzi DP).

60 Ibid 538–9 (Micalizzi DP).

61 Ibid 539 (Micalizzi DP).

62 *Corporations Act 2001* (Cth) s 420A(1).

63 Cf *Pasminco* (2002) 41 ACSR 511, 539 (Micalizzi DP).

It is difficult to argue with the minority's view that there should have been an independent expert valuation of the company's assets.[64] This would seem to be a sensible precaution to avoid concerns in cases where there is reason to doubt that the administrators are acting in good faith. A requirement for an independent assessment of the company's situation would also be appropriate if the High Court's principles in *Gambotto v WCP Ltd*[65] ('*Gambotto*') were to apply, and for the purposes of determining whether the takeover provisions should apply to the company.[66]

Subject to it being correct that shareholders would not receive any return from a winding up, the principles discussed above support the creditors' entitlement to be issued shares and to use the existing company to trade to minimise their losses.[67]

2 *Shareholder Spread*

The administrators proposed that, if the planned reconstruction of Pasminco was successful, the number of pre-administration shareholders could be used to satisfy the ASX requirement that a listed company have at least 500 shareholders who each hold ordinary shares worth at least A$2000.[68] The majority considered that the shareholder spread was an asset of the company that could be used by the creditors,[69] whereas the minority considered that the shareholder spread was only an asset of the shareholders.[70]

Ordinarily, the question whether the number of shareholders in a company is an asset in its own right would not be raised. Rather, in the context of a solvent company with a share capital, it is the funds that shareholders inject into the company that is the important factor. However, when considering whether to invest in a company, the number of shareholders may be one of the factors that investors may take into account. This is because, whether or not the company's shares are traded on the ASX, they will be a more attractive investment if there is a liquid market in which the shares can be sold easily to existing or prospective shareholders.

Notwithstanding these investment considerations, it is difficult to see how the existence and number of shareholders could be an asset of any person except the company. When shareholders purchase a share, they receive an asset that is a kind of intangible personal property known as a chose in action (the value of which is determined by the rights attaching to the shares). Unless the company's constitution or the terms on which the shares are issued provide otherwise, shareholders do not have rights to specific assets of the company. Instead, their economic rights comprise the payment of any dividends and where possible a

64 Ibid.
65 (1995) 182 CLR 432.
66 See below in this Part and Part IV respectively for discussion of both of these.
67 See below Part IV for discussion of the relative rights of creditors and shareholders in a voluntary administration.
68 ASX Listing Rule 1.1, Condition 7.
69 *Pasminco* (2002) 41 ACSR 511, 532 (Byrne P and Lee).
70 Ibid 534 (Micalizzi DP).

return of capital on winding up. It would consequently be incongruous for shareholders to retain rights in a specific asset of the company, particularly one that represents their contribution to the company for which they have been already compensated through the issue or transfer of the share.

This reasoning does not take into account the view that it could be considered 'unfair' to shareholders for creditors to be able to capitalise on the existence of the pre-administration shareholders without in some way compensating them. Except for any other rights that they may have under the law (discussed below), there would appear to be no steps that the shareholders could take to avoid the shareholder spread being used to restore the company's listing on the ASX. This is because, until the shares are requoted or at least have some value, the shareholders are unable to sell their shares.[71]

It should be noted that the proposal for Pasminco to be listed would depend upon the shares having sufficient value for each shareholder to hold shares worth at least A$2000. This assumes that the company has traded out of difficulty, with a restoration of at least part of the value of the pre-administration shareholders' investment. In these circumstances, it would be difficult to see how the shareholders would suffer a loss from the proposed use of Pasminco as a corporate entity and their shareholdings to restore the company's listing.

B Do the Shareholders Have Any Further Rights?

Given that general company law principles support the use of the corporate entity and its shareholdings, the only remaining question is whether the law of oppression or any other *Corporations Act* provisions could assist the pre-administration shareholders.

1 *Oppression*

The issue of oppression is only briefly dealt with by the majority. They point out that, although the court[72] can terminate a deed of company arrangement on the grounds that it is oppressive to at least one creditor or contrary to the interests of the creditors as a whole,[73] there is no similar ground for a deed that is oppressive to shareholders.[74] However, the court has a broad discretion to terminate the deed on the application of 'any other interested person',[75] for example, if the provisions of Part 5.3A of the *Corporations Act* are being abused[76] or 'for some other reason'.[77] Reinforcing the focus on creditor rather than shareholder rights, the Australian Law Reform Commission stated in the context of its recommendations on the court's supervisory role in the voluntary

71 Although it may be possible for the shareholders to arrange for their shares to be cancelled, this would not make any economic sense.

72 Primarily, the Federal Court or a Supreme Court of a State or Territory: *Corporations Act 2001* (Cth) s 58AA(1).

73 *Pasminco* (2002) 41 ACSR 511, 523 (Byrne P and Lee); *Corporations Act 2001* (Cth) s 445D(1)(f).

74 *Pasminco* (2002) 41 ACSR 511, 523 (Byrne P and Lee); *Corporations Act 2001* (Cth) s 447A.

75 *Corporations Act 2001* (Cth) ss 445D(2)(c), 447A(4)(f).

76 *Corporations Act 2001* (Cth) s 447A(2)(b).

77 *Corporations Act 2001* (Cth) ss 445D(1)(g), 447A(2)(c).

administration procedure that a 'creditor, for example, would be an interested person as *may be* a member of the company'.[78]

ASIC argued that it would be more appropriate for the administrators' proposal to proceed by way of scheme of arrangement, due to the requirement for the court to take shareholders' interests in such a scheme into account and the opportunity for ASIC and the shareholders to represent such interests.[79] However, the majority responded that 'it seems unreasonable to suggest that the court would regard the suggested reconstruction as oppressive of shareholders, whether it was conducted by deed or by scheme'.[80]

The principles underlying the oppression remedy are similar whether shareholders bring an action under the general law or under s 232 of the *Corporations Act.* Under s 232, the court could make an order if the conduct of Pasminco's affairs[81] is 'contrary to the interests of the members as a whole' or 'oppressive to, unfairly prejudicial to, or unfairly discriminatory against, a member'.[82]

Although there do not appear to be any cases that are based upon similar facts, it has been held that the test for oppression in a commercial company is that of 'commercial fairness judged objectively as by a commercial bystander'.[83] At the time of the *Pasminco* case, it would be difficult to establish that the issue of shares to the creditors would be oppressive to the pre-administration shareholders. This is because, assuming that the company is in fact insolvent, shareholders could have no reasonable expectation of any return in the immediate future. However, the issue of shares to creditors could allow them to trade the company out of financial difficulty, with a potential return to shareholders. This would likely meet the standard of 'commercial fairness' to the shareholders.

Even if the administrators' conduct was found to be oppressive, it is difficult to see what appropriate order could be made that would benefit the shareholders. An order to wind up the company[84] would not financially benefit the shareholders due to the company's inability to pay its debts. Similarly, an order regulating the conduct of the company's affairs in the future,[85] or requiring the

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78 Australian Law Reform Commission, *General Insolvency Inquiry*, Report No 45 (1988) vol 1, 34 (emphasis added).

79 *Pasminco* (2002) 41 ACSR 511, 528–9 (Byrne P and Lee). This issue is discussed in more detail below Part IV.

80 Ibid 529 (Byrne P and Lee).

81 The conduct of the administrator and the ownership of shares in Pasminco are both covered by the definition of the 'affairs of a body corporate': see *Corporations Act 2001* (Cth) s 53(d), (e).

82 *Corporations Act 2001* (Cth) s 232(a), (d), (e). The administrator's conduct could alternatively be classified as 'an actual or proposed act or omission by or on behalf of a company': *Corporations Act 2001* (Cth) s 232(b).

83 See *Morgan v 45 Flers Avenue Pty Ltd* (1986) 10 ACLR 692, 704; *Coombs v Dynasty Pty Ltd* (1994) 14 ACSR 60, 99; *Dynasty Pty Ltd v Coombs* (1995) 13 ACLC 1290, 1296.

84 *Corporations Act 2001* (Cth) s 233(1)(a).

85 *Corporations Act 2001* (Cth) s 233(1)(c).

administrator to (or not to) do a particular act,[86] would not likely lead to a successful outcome due to the need for the support of the creditors.[87]

2 *The* Gambotto *case*

If the principles in the High Court's decision in *Gambotto*[88] could be applied to the *Pasminco* circumstances, they would be of assistance to the shareholders. However, for the reasons set out below, it is unlikely that they would be found to apply.

In *Gambotto*, the majority of the High Court decided that an amendment to a company's constitution to expropriate the minority shareholders' shares or a valuable proprietary right is not valid unless it is made for a proper purpose and not oppressive to the minority shareholders.[89] For these principles to assist the Pasminco shareholders, they would need to overcome two obstacles. First, the *Gambotto* principles would need to apply to actions by creditors in circumstances other than an amendment to the company's constitution. Implied support for this may be drawn from statements, both in case law[90] and in explanatory material prior to legislative changes,[91] that the *Gambotto* principles do not apply to statutory procedures involving compulsory acquisition of shares. This points to the High Court's principles having a broader reach than the particular circumstances in *Gambotto*. Second, there would need to be a finding that the creditors had expropriated a valuable proprietary right of the shareholders. As argued above, it would be difficult to establish that the creditors' use of the corporate entity and shareholder spread in an insolvency context would do this.

In the unlikely event that the above two obstacles were overcome, it could be argued that the proposal was invalid on the basis that neither limb of the *Gambotto* test would be satisfied. In relation to the 'proper purpose' limb, if the majority in *Gambotto* did not consider a A$4 million tax advantage in that case to be sufficient,[92] it is unlikely that the estimated A$200 000 cost saving of using a deed of company arrangement[93] would satisfy the requirement. Even McHugh J, who considered there to be a proper purpose in *Gambotto*,[94] indicated that the power could not be used for administrative convenience or cost.[95]

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86 *Corporations Act 2001* (Cth) s 233(1)(i), (j).

87 *Pasminco* (2002) 41 ACSR 511, 513 (Byrne P and Lee), 535 (Micalizzi DP).

88 (1995) 182 CLR 432.

89 Ibid 445 (Mason CJ, Brennan, Deane and Dawson JJ).

90 See, eg, *Winpar Holdings Ltd v Goldfields Kalgoorlie Ltd* (2000) 176 ALR 86, 95–7.

91 See Explanatory Memorandum, Company Law Review Bill 1997 (Cth) [12.25] (for selective capital reductions under *Corporations Act 2001* (Cth) pt 2J.1, div 1) and Corporate Law Economic Reform Program, above n 5, 29 (for compulsory acquisitions under *Corporations Act 2001* (Cth) ch 6A).

92 *Gambotto* (1995) 182 CLR 432, 448 (Mason CJ, Brennan, Deane and Dawson JJ).

93 *Pasminco* (2002) 41 ACSR 511, 536 (Micalizzi DP), 527 (Byrne P and Lee). The comparative cost savings are discussed in detail below Part IV.

94 *Gambotto* (1995) 182 CLR 432, 459 (McHugh J).

95 Ibid 455 (McHugh J).

According to the majority in *Gambotto*, the second limb of the test required both substantive and procedural fairness.[96] It is unlikely that there would have been procedural fairness as neither Pasminco's shareholders, nor the directors who were seeking to represent their interests, had access to information on the value of Pasminco's assets.[97] In addition, the majority in *Gambotto* would have required the shares to be valued by an independent expert.[98] The substantive fairness issue would be more difficult to argue given the shareholders' lack of access to financial information. However, it should be noted that the majority considered that the current market value may be insufficient, allowing future improvements in price to be taken into account.[99]

3 *Winding Up*

The members could seek to apply for a winding up order under s 461 of the *Corporations Act*. For the reasons discussed above, it seems unlikely that a court would give such an order based upon the oppression ground.[100] Similarly, an order based on the 'just and equitable' ground[101] would not appear probable on the facts in *Pasminco*. In any case, the court would likely be required to adjourn a winding up application on the basis that it would be satisfied that it is in the interests of the creditors for the administration to continue.[102] Winding up Pasminco would not appear to be in the shareholders' economic interests as they would not receive any return on liquidation.

4 *Abuse of Voluntary Administration Process*

Abuse of the voluntary administration process may be dealt with under either the *Corporations Act* or the general law. Shareholders can apply to the court for the termination of a deed of company arrangement.[103] The grounds for termination would be unlikely to assist the Pasminco shareholders, as they generally relate to issues that are material to the creditors.[104] The court also has a general discretion to terminate the deed 'for some other reason'.[105] However, given that the interests of shareholders are subordinated to creditors in the voluntary administration,[106] it would not be likely that a court would terminate a deed that was approved by creditors and was in their interests.

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96 Ibid 446 (Mason CJ, Brennan, Deane and Dawson JJ).

97 *Pasminco* (2002) 41 ACSR 511, 515–17 (Byrne P and Lee), 538 (Micalizzi DP). The disclosure tests put forward by McHugh J would similarly not have been met: see *Gambotto* (1995) 182 CLR 432, 459–60 (McHugh J).

98 *Gambotto* (1995) 182 CLR 432, 446 (Mason CJ, Brennan, Deane and Dawson JJ).

99 Ibid 447 (Mason CJ, Brennan, Deane and Dawson JJ).

100 *Corporations Act 2001* (Cth) s 461(f) or (g).

101 *Corporations Act 2001* (Cth) s 461(k).

102 *Corporations Act 2001* (Cth) s 440A(2).

103 *Corporations Act 2001* (Cth) ss 445D, 445G.

104 See, eg, *Corporations Act 2001* (Cth) s 445D(1)(a)–(c), (f).

105 *Corporations Act 2001* (Cth) ss 445D(1)(g). See also s 445G, which allows the court to terminate the deed where there is doubt that it complies with *Corporations Act 2001* (Cth) pt 5.3A.

106 Austin and Brown, above n 56, 196.

Alternatively, the shareholders could seek to argue that the administrators had breached their statutory duty to act in good faith in the best interests of the company.[107] It has also been argued that an administrator owes fiduciary duties to the company.[108] Apart from the procedural issues that shareholders would confront in bringing an action for a breach of duty to the company, they would also face the difficulties that directors have a duty to take into account the interests of creditors in an insolvency situation[109] and that termination of the deed would be unlikely to be a remedy for any breach.[110]

IV TAKEOVER RULES FOR COMPANIES IN ADMINISTRATION

This Part examines the issue whether the Panel should have granted the takeover exemption for the administrators' proposal. The following matters are discussed at the outset to enable the justification for the exemption to be evaluated and to place the Panel's decision in its regulatory context. First, this Part examines the alternative routes that were available to the administrator under the takeover legislation. Second, the rationale for the takeover provisions and existing exceptions in the legislation are discussed to assess the circumstances in which the takeover provisions would ordinarily apply. Third, the purpose and effect of the voluntary administration provisions are examined to determine the efficacy of allowing acquisitions under a deed of company arrangement to be exempted from the takeover provisions.

A Alternatives Available to Administrators

The majority identified three ways to implement the administrators' proposal consistent with the takeover provisions.[111] These involved obtaining an exemption either through approval by the creditors and the court for a creditors' scheme of arrangement under Part 5.1 of the *Corporations Act*,[112] through approval by the shareholders,[113] or through approval by ASIC (or, on review, the Panel).[114] The cost of the first two options was compared with the final option of seeking an ASIC exemption in relation to shares issued under a deed of company arrangement.[115] It was estimated that a scheme of arrangement would cost an

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107 See *Corporations Act 2001* (Cth) s 9, 'officer' (paragraph (d)) and ss 181, 184. Note shareholders do not have standing to apply for the removal of the administrator under *Corporations Act 2001* (Cth) s 449B.

108 See generally Austin and Brown, above n 56, 193–9 and David J Kerr, 'Independence of Company Administrators Appointed Pursuant to Part 5.3A of the *Corporations Law*' (2000) 12 *Australian Insolvency Journal* 4, 8.

109 See above n 57.

110 Austin and Brown, above n 56, 198–9.

111 *Pasminco* (2002) 41 ACSR 511, 514 (Byrne P and Lee).

112 *Corporations Act 2001* (Cth) s 611, item 17.

113 *Corporations Act 2001* (Cth) s 611, item 7.

114 *Corporations Act 2001* (Cth) ss 655A, 656A.

115 It is not clear whether these figures take into account the costs involved in an ASIC exemption and, as applicable here, subsequent Panel proceedings.

additional A$200 000 (or about 0.006 per cent of the debts owed to the creditors) compared with a deed of company arrangement.[116] The shareholder approval option was slightly cheaper at an additional A$150 000.[117] However, the shareholder approval option was not attractive to the creditors, because they did not want to give shareholders the power to veto the transaction.[118]

There are other reasons why a deed of company arrangement would be more attractive to creditors than a creditors' scheme of arrangement.[119] The key advantage of a deed is its less onerous approval requirements. A deed can be approved by a 50 per cent majority (by number and value)[120] of all creditors without necessarily involving a court. In contrast, a creditors' scheme would require separate creditors' meetings for each class (with approval by 75 per cent by value and 50 per cent by number) and court approval.[121] The deed of company arrangement also has streamlined information requirements and does not give a formal role to ASIC or the company's shareholders.[122] In contrast, before a scheme of arrangement can be approved by the court, either ASIC must have provided a written statement that it has no objection to the arrangement[123] or the court must be satisfied that the arrangement has not been proposed for the purpose of enabling any person to avoid the takeover provisions.[124] Even before the application was made to ASIC for the takeover exemption, there would have been uncertainty as to whether the creditors' scheme could have satisfied these requirements.

B Rationale for Takeover Provisions and Existing Exceptions

In exercising its takeover exemption and modification powers, ASIC is required to consider the purposes of the takeover provisions set out in s 602 of the *Corporations Act*.[125] The first purpose is to ensure that the acquisition of control over voting shares occurs in 'an efficient, competitive and informed market'.[126] Another key purpose is to require that, as far as practicable, shareholders have 'a reasonable and equal opportunity to participate in any benefits accruing to the holders through any proposal under which a person would acquire a substantial interest in the company'.[127] The remaining purposes

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116 *Pasminco* (2002) 41 ACSR 511, 536 (Micalizzi DP), 527 (Byrne P and Lee).

117 Ibid 527 (Byrne P and Lee).

118 Ibid 513 (Byrne P and Lee).

119 Ibid 522–3 (Byrne P and Lee). The essential differences between them are usefully set out in a table. See also Colin Anderson and David Morrison, 'Voluntary Administrations and Their Effect on the Use of Schemes of Arrangement' (1994) 2 *Insolvency Law Journal* 195.

120 *Corporations Act 2001* (Cth) s 439C.

121 *Corporations Act 2001* (Cth) s 411(4).

122 See *Pasminco* (2002) 41 ACSR 511, 522–3 (Byrne P and Lee).

123 See Australian Securities and Investments Commission, *Policy Statement 60 Schemes of Arrangement — s 411(17)* (1999) [8], [20]. Before giving such a statement, ASIC must be satisfied that shareholders receive the same amount of disclosure as they would under the takeover provisions.

124 *Corporations Act 2001* (Cth) s 411(17).

125 *Corporations Act 2001* (Cth) s 655A(2).

126 *Corporations Act 2001* (Cth) s 602(a).

127 *Corporations Act 2001* (Cth) s 602(c). Sections 606(b) and (c) are known as the 'Eggleston principles': see Company Law Advisory Committee, *Report to the Standing Committee of Attorneys-General on*

require shareholders and directors to be given sufficient information so they can assess the proposal and provide an appropriate procedure prior to any compulsory acquisition of shares.[128]

The takeover provisions are designed to protect the interests of shareholders where the person or persons with power to control a company changes. They do this by ensuring that, where a company changes control, all shareholders have the opportunity to share in the benefits. To ensure that the provisions are triggered before a change in control, there is a prohibition against a person acquiring more than 20 per cent of the voting power in the company.[129] An exception to the prohibition must apply before a person can proceed any further.[130] Given the costs of compliance, the provisions do not apply to companies that are not listed on the ASX and have 50 or fewer members.[131] The broad and often complex definitions underpinning the takeover provisions are designed to cover all circumstances in which a person may have control over shares.[132] As discussed in Part II of this article, the administrators' proposal would contravene the takeover prohibition as a result of the proposed agreements between the creditors controlling share disposal and relating to the conduct of Pasminco's affairs.

It is useful to briefly examine the existing takeover exceptions in the *Corporations Act*, to place the decision to provide the *Pasminco* exemption in context. While not determinative of the question whether a new kind of exemption should be granted, such an examination illustrates the circumstances in which the legislature currently allows transactions that would otherwise breach the takeover provisions. The existing takeover exceptions have been grouped into five categories to assist in their evaluation.

First, there are a number of takeover-related and other technical exceptions.[133] The main exceptions are based upon the acquisition resulting from a takeover bid that is sanctioned by the legislation.[134] Others rely upon, for example, shareholders having the opportunity to approve the acquisition[135] or sell their shares in an anonymous transaction on the ASX,[136] or having time to assess the impact of the acquisition.[137] Another technical exception applies to acquisitions

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Disclosure of Substantial Shareholdings and Takeovers (1969). For a recent discussion of the continuing relevance of the Eggleston principles, see Justin Mannolini, 'Convergence or Divergence: Is there a Role for the Eggleston Principles in a Global M&A Environment?' (2002) 24 *Sydney Law Review* 336, 336–40, 360.

128 *Corporations Act 2001* (Cth) s 602(b), (d).

129 *Corporations Act 2001* (Cth) s 606.

130 *Corporations Act 2001* (Cth) s 611. One of the key exceptions is an offer to purchase all of the remaining shares under the prescribed procedure: see item 1.

131 *Corporations Act 2001* (Cth) ss 602(a), 606.

132 See, eg, *Corporations Act 2001* (Cth) ss 12, 606–10.

133 See, eg, *Corporations Act 2001* (Cth) s 611, items 1–4, 7, 9, 14, 16. There are also exceptions in the *Corporations Regulations 2001* (Cth) under item 20, which apply to certain types of bodies corporate and public officials: at regs 6.2.01, 6.2.02.

134 *Corporations Act 2001* (Cth) s 611, items 1, 4.

135 *Corporations Act 2001* (Cth) s 611, item 7.

136 *Corporations Act 2001* (Cth) s 611, items 2, 3, 16.

137 *Corporations Act 2001* (Cth) s 611, item 9.

'through operation of law'.[138] This exception is designed to cover acquisitions that are required by legislation, such as under a court order. In the *Pasminco* case, the administrators' proposal was only one of the options available to them and was not a necessary result of the application of a law.

Second, the fundraising exceptions are designed to facilitate the ability of companies to obtain investment through issuing shares in certain limited situations. The exceptions with the strongest rationale from a takeover standpoint are share issues that are equally available to existing shareholders under rights issues and dividend reinvestment plans.[139] These give shareholders the opportunity to avoid having their voting power diluted by taking up the shares being offered.

Another fundraising exception applies to share issues by companies before they start to carry on business and borrow money,[140] allowing companies to boost their capital prior to commencing operation. Although such share issues would affect the position of the initial shareholders in the company, it is arguable that the risk is acceptable given that the initial shareholders are likely to have been involved in the setting up of the company and thus be in a position to protect their interests.

The remaining fundraising exceptions apply to issues to a promoter under an initial public offering, or an underwriter in any fundraising, where there is appropriate disclosure to investors. Both exceptions require the shares to be issued under a fundraising document that discloses the effect that it would have on the person's voting power in the company.[141] This ensures that existing and potential shareholders are informed of the consequences of the share issue.

Third, there are two types of exceptions relating to reconstructions. As discussed earlier in this Part, a creditors' scheme of arrangement would have been an alternative way for the Pasminco administrators to proceed.[142] This takeover exception could be justified based upon the requirement for the court to approve the scheme after taking into account the interests of shareholders. However, the more onerous approval requirements and increased costs made this a less attractive option than a deed of company arrangement. The exception for share buy-backs[143] is a technical one, as the company briefly acquires an interest in shares it buys back. However, the shares are immediately cancelled after the transfer to the company is registered.[144]

Fourth, there are two limited insolvency exceptions that apply for the benefit of finance providers and liquidators selling an insolvent company's business or property. Under the first exception, creditors could exercise a power under a mortgage, charge or other security obtained in the ordinary course of their

138 *Corporations Act 2001* (Cth) s 611, item 15.
139 *Corporations Act 2001* (Cth) s 611, items 10–11.
140 *Corporations Act 2001* (Cth) s 611, item 8.
141 *Corporations Act 2001* (Cth) s 611, items 12–13.
142 *Corporations Act 2001* (Cth) s 611, item 17.
143 *Corporations Act 2001* (Cth) s 611, item 19.
144 *Corporations Act 2001* (Cth) s 257H(3).

business and on commercial terms.[145] For example, this allows providers of finance to acquire shares that have been used by the borrower as security for a loan.

The second insolvency exception applies where a liquidator accepts shares in another company as consideration for the sale of the insolvent company's business or property.[146] This exception raises interesting takeover policy issues, as it could result in the shareholders of the insolvent company to which the liquidator has been appointed obtaining control of the other company that is buying the insolvent company's property. However, the procedure only requires approval by the shareholders of the insolvent company selling the property, not those of the company that could potentially be taken over through the transfer of its shares.[147] This exception can perhaps only be explained in terms of its facilitation of the liquidation of the company.

Fifth, ASIC has very broad exemption and modification powers in relation to takeovers in s 656A of the *Corporations Act*.[148] ASIC's powers give substantial flexibility to takeover regulation, as the rules can be modified to remove any anomalies that may arise from the operation of the legislation or its application to the particular circumstances of the case. Although the powers are principally used to remove technical difficulties arising from the legislation, they can be used to exempt a particular class of companies on the basis that the protection of the takeover provisions is not needed in those circumstances. The High Court has upheld the broad nature of ASIC's powers.[149]

C Voluntary Administration

The voluntary administration provisions in Part 5.3A of the *Corporations Act* were implemented in 1993[150] to provide a relatively inexpensive and quick procedure for determining whether a company can be traded out of financial difficulty.[151] The object of Part 5.3A is specifically set out in legislation, namely

> to provide for the business, property and affairs of an insolvent company to be administered in a way that:
> (a) maximises the chances of the company, or as much as possible of its business, continuing in existence; or

145 *Corporations Act 2001* (Cth) s 611, item 6.

146 *Corporations Act 2001* (Cth) ss 507, 611, item 18.

147 *Corporations Act 2001* (Cth) s 507(2).

148 These powers must be exercised after considering the purposes of the takeover provisions. See above nn 126–32 and accompanying text.

149 See *Australian Securities and Investments Commission v DB Management Pty Ltd* (2000) 199 CLR 321, 340–2 (Gleeson CJ, Gaudron, Gummow, Hayne and Callinan JJ). In that case, the High Court upheld ASIC's exercise of its powers to allow the compulsory acquisition of a class of securities that at the time was not possible under the legislation.

150 The *Corporate Law Reform Act 1992* (Cth) inserted the voluntary administration provisions on 23 June 1993.

151 See Australian Law Reform Commission, above n 78, 29–30.

(b) if it is not possible for the company or its business to continue in existence — results in a better return for the company's creditors and members than would result from an immediate winding up of the company.[152]

An administration will usually result in one of three outcomes, namely the company and its administrator[153] executing a deed of company arrangement, the creditors ending the administration, or the creditors resolving to wind up the company.[154] During the administration, the powers of other company officers are suspended[155] and only the administrator can deal with the company's property.[156] Proceedings and enforcement processes also generally cannot be brought without the administrator's consent or the leave of the court.[157] After investigating the company's business, property, affairs and financial circumstances, the administrator is required to form an opinion about whether it would be in the interests of the company's creditors for each of the above three outcomes to occur.[158]

Two meetings of creditors are held during the administration, with the second meeting deciding its outcome.[159] Only creditors vote on whether the company should execute a deed of company arrangement and, if they do so, the deed must be executed.[160] An executed deed binds creditors,[161] the company, its officers and shareholders, and the deed's administrator.[162] However, the company is only released from its debts to the extent that the deed provides for the release and the creditor is bound by the deed.[163]

This brief overview of the voluntary administration provisions demonstrates the lack of shareholder participation in the procedure. The focus on the interests of creditors is reflected in the Australian Law Reform Commission report that led to the introduction of the voluntary administration procedure.[164] Apart from the object of providing a better return for members (which is consistent with providing a better return for creditors), Part 5.3A principally refers only to the

152 *Corporations Act 2001* (Cth) s 435A.

153 Two or more administrators may be appointed for the company or deed of company arrangement: *Corporations Act 2001* (Cth) ss 451A, 451B.

154 *Corporations Act 2001* (Cth) s 435C(2).

155 *Corporations Act 2001* (Cth) s 437C. However, the directors are required to assist the administrator under s 438B.

156 *Corporations Act 2001* (Cth) s 437D.

157 *Corporations Act 2001* (Cth) pt 5.3A, div 6. However, there are exceptions for certain charge holders and other creditors in div 7.

158 *Corporations Act 2001* (Cth) s 438A.

159 *Corporations Act 2001* (Cth) ss 436E, 439A.

160 *Corporations Act 2001* (Cth) ss 444A, 444B.

161 Except for secured creditors and the owner or lessor of property: *Corporations Act 2001* (Cth) s 444D. However, the court may limit their rights under s 444F.

162 *Corporations Act 2001* (Cth) s 444G.

163 *Corporations Act 2001* (Cth) s 444H.

164 See, eg, Australian Law Reform Commission, above n 78, 28–9, 34, 37, 56, 63. Explanatory Memorandum, Corporate Law Reform Bill 1992 (Cth) [22] also includes giving protection to the rights of creditors as a key element of the pt 5.3A procedure.

effect that the administration has on the shareholders[165] and their ability to apply for court intervention in the process.[166] It is only in the case of the court's supervision of the administrator that the legislation specifically provides for the interests of shareholders to be taken into account. That is, the court can make any order it thinks fit if the administrator's management of the company's business, property or affairs is prejudicial to the interests of some or all of the company's creditors or members.[167] Although there do not appear to have been any cases in which this provision has been used to address prejudice to members, it has been noted that the provision could be used where an administrator has failed to act impartially.[168]

D Should Takeover Rules Apply to Companies Under Administration?

1 *Policy Analysis*

It can be seen from the above analysis of the takeover exceptions that insolvency in itself does not form the basis of any existing legislative exemption. The closest exception to the *Pasminco* situation is the creditors' scheme of arrangement, which a court must approve after being satisfied that the purpose of the scheme is not to avoid the takeover provisions.[169]

Nevertheless, the *Pasminco* exemption can be justified on general principles. The takeover provisions are based upon ensuring that the same benefits are offered to all shareholders in a change of control situation. One of the bases for this principle is that the person purchasing shares to take over the company is paying a higher price for the shares in order to achieve control (referred to as 'the control premium'). As control of the company is considered to be an asset of all shareholders, the takeover provisions require this control premium to be distributed evenly amongst the shareholders by making the same offer available to all shareholders.

If the shareholders would not receive any return of their investment because the company's debts to creditors cannot be repaid, the company can be operated in the interests of the creditors rather than the shareholders.[170] Consequently, under the law, control of the company passes from the shareholders to the creditors.[171] Consistent with the purposes of the voluntary administration provisions, the administrators' proposal in *Pasminco* involved restructuring an insolvent company so that it could continue operating.

165 Namely, the inability to transfer shares, the administrator's ability to report on offences by members and the effect of the deed of company arrangement: *Corporations Act 2001* (Cth) ss 437F, 438D, 444G.

166 Namely, for the court to invalidate a deed of company arrangement, remove an administrator or fill a vacancy in the office, or to review the administrator's remuneration: *Corporations Act 2001* (Cth) ss 445G, 447E, 449C, 449D, 449E.

167 *Corporations Act 2001* (Cth) s 447E(1)(a).

168 See Austin and Brown, above n 56, 195.

169 *Corporations Act 2001* (Cth) s 411(17)(a). Alternatively, ASIC must have given a statement that it has no objection under *Corporations Act 2001* (Cth) s 411(17)(b), for which it similarly considers the takeover provisions: see above n 123.

170 See above Part III.

171 *Pasminco* (2002) 41 ACSR 511, 527 (Byrne P and Lee).

In these circumstances, it is appropriate that the creditors be able *in fact* to take control of the company by swapping their debt for equity. It is difficult to see that there are any benefits that the shareholders could rightly claim from the proposed arrangements in which the creditors would be forgiving debts to the company. Accordingly, the rationale for the takeover provisions does not appear to be relevant to the *Pasminco* situation.

2 *Difficulty with Duration of Panel Exemption*

Although a takeover exemption was justifiable at the time that Pasminco was in an insolvency situation, there is a time at which the takeover provisions should apply if the company is in fact traded back to financial health. The difficulty is establishing what that time should be. It could be argued that, technically, Pasminco would no longer be insolvent once the deed of company arrangement eliminated the company's debts. In light of this, it is arguable that the exemption should only apply for a reasonable time following the execution of the deed of company arrangement. The proposal in *Pasminco* involved agreements between the creditors that would breach the takeover provisions for the duration of the restructure, which was estimated to be between one and 10 years.[172]

It is difficult to justify granting a takeover exemption that would last up to 10 years. It may be argued that detriment to future shareholders could be ameliorated through appropriate disclosure of the effect of the exemption. However, it seems inappropriate to remove the shareholder protections in the takeover provisions for that length of time. Assuming that the company was at that stage trading profitably, the interests of the shareholders as a whole would become relevant. This is particularly the case if new shareholders were investing in the company or if Pasminco's shares could be traded on the ASX. In either case, the company would meet the threshold for the takeover provisions to apply.[173]

3 *When is an Exemption Appropriate?*

A difficulty with the *Pasminco* decision is that it is not easy to distil a policy for when the relief should be available in future cases. The majority considered that it would be anomalous for shareholders to be required to approve the proposal as:

- the shareholders' shares had no value, compared with the estimated A$3 billion of creditors' money involved in the reconstruction;[174]
- the takeover provisions should not apply to acquisitions of shares by the creditors, as they had legitimately taken control of Pasminco;[175]

172 Ibid 520 (Byrne P and Lee).

173 *Corporations Act 2001* (Cth) s 606(1)(a)(ii). The threshold of more than 50 members for unlisted companies would be met assuming that Pasminco retained the pre-administration shareholders.

174 *Pasminco* (2002) 41 ACSR 511, 527 (Byrne P and Lee). Giving shareholders a vote was considered to be unreasonable in that it would grant them a windfall.

175 Ibid.

- making a takeover bid 'would not address the issues of sharing in the benefits which a takeover is designed to preserve';[176] and
- the administrators were 'essentially answerable only to the company's creditors' and the shareholders had 'no interest which the administrators are obliged to preserve or respect'.[177]

The key basis for the relief consequently appears to be the fact that the Pasminco shareholders would not receive any return on winding up. This conclusion would depend upon a valuation of the company's assets. If the company is being wound up, a liquidator appointed by the court would determine to what extent the creditors would be paid. In the context of an administration, it is the administrator who does these valuations. As discussed earlier, there is a potential for misuse of the voluntary administration provisions. This suggests that an independent valuation may be appropriate.

It would not be appropriate to include a legislative exception due to this uncertainty as to when the basis for the relief would be satisfied. A legislative amendment would in any case be premature, as there has only been one instance where this relief has been sought. Such a step could only be taken after experience with a number of cases, demonstrating that the relief had not led to any abuse of shareholder interests.

This conclusion is consistent with the recommendation of the Legal Committee of the Companies and Securities Advisory Committee in its June 1998 report, *Corporate Voluntary Administration*. The Committee considered whether there should be an exemption from the takeover provisions for acquisitions of shares pursuant to a voluntary administration. It decided against such an exemption on the following grounds:[178]

- most companies under voluntary administration would not be subject to the takeover provisions as they would not satisfy the threshold of more than 50 members for unlisted companies;[179]
- as the test for insolvency is based upon cash flow rather than assets and liabilities, it is possible that the shares may still have 'an intrinsic underlying value for shareholders'[180] and thus the issue of a control premium may still be relevant; and
- ASIC has the power to modify the takeover provisions, 'while still ensuring that shareholders are not unduly deprived of reasonable information or an opportunity to consider a proposal under which control of the company would change'.[181]

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176 Ibid.

177 Ibid.

178 Legal Committee of the Companies and Securities Advisory Committee, *Corporate Voluntary Administration* (1998) [9.9].

179 *Corporations Act 2001* (Cth) s 606(1)(a)(ii).

180 Legal Committee of the Companies and Securities Advisory Committee, above n 178. In the *Pasminco* case, the administrators had concluded that the company's liabilities materially exceeded its assets: *Pasminco* (2002) 41 ACSR 511, 513 (Byrne P and Lee).

181 Legal Committee of the Companies and Securities Advisory Committee, above n 178.

The Committee also noted that it had received a submission raising a concern that such an exemption 'might encourage companies to use voluntary administration as a means of effecting a change in control without complying with the takeover requirements'.[182] This concern partly arises from the fact that the voluntary administration procedure can be activated if the board of directors resolves that 'in the opinion of the directors voting for the resolution, the company is insolvent, or *is likely to become insolvent at some future time*'.[183] It is supported by cases illustrating that the voluntary administration provisions are open to abuse.[184]

In light of this, it would be more appropriate to retain the current process of requiring an ASIC exemption in similar circumstances, where one of the other legislative exceptions is not being used. Disappointingly, the Panel's decision does not give firm guidance on what policy ASIC should apply. It may be that the *Pasminco* scenario is unlikely to reoccur frequently. However, if it did, ASIC would need to develop an appropriate policy for any future applications. It would be desirable for this to be done in consultation with the Panel.

V CONCLUSION

The *Pasminco* case illustrates the Takeovers Panel's willingness to exercise its powers to make commercial decisions. The takeover exception granted was innovative, and has important ramifications for takeover policy in the future.

The majority of the Panel made a pragmatic decision. Faced with the prospect of a significant Australian company being wound up, with consequences for its employees and the economy generally, the majority of the Panel decided to facilitate a restructuring of the company that has to date allowed it to continue to operate. Whereas a winding up would have left shareholders with nothing and creditors with substantial losses from debts of nearly A$2.9 billion, the restructure has the potential to minimise creditor losses and give shareholders a return in the future.[185]

The administrators' proposal to use the existing shareholders in a future attempt to restore the company's listing on the ASX was also novel. Although the potential use of the corporate entity and shareholder spread for the benefit of the creditors may appear to be a harsh outcome for the shareholders, the

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182 Ibid [9.8].

183 *Corporations Act 2001* (Cth) s 436A(1)(a) (emphasis added).

184 See, eg, *Cresvale Far East Ltd (in liq) v Cresvale Securities Ltd* (2001) 37 ACSR 394 and, generally, Austin and Brown, above n 56, 179.

185 Although Pasminco made a A$411 million loss in the year to 30 June 2002, it was announced on 1 November 2002 that the company had a positive cash flow of A$19.1 million in the second half of the year. Under the restructuring plan announced on 7 October 2002, Pasminco's creditors will exchange their debt for equity in a new company (Pasminco Resources), which is expected to be subject to a public float and listing on the ASX in early 2003: see Pasminco Ltd, 'Pasminco Deeds of Company Arrangement Signed' (Press Release, 7 October 2002), <http://www.pasminco.com.au/index.asp?link_id=7.1025> at 13 November 2002. Despite the protracted proceedings, it appears that creditors will not be using the corporate entity of Pasminco and its shareholder spread.

majority's decision on this issue is consistent with general company law principles. Concerns about the inability of shareholders to prevent creditors taking over the company are understandable. However, where a company is insolvent, the law clearly operates for the benefit of creditors, and shareholders, in effect, no longer have a say in what happens to the company's assets.

One of the benefits of the Panel's expanded jurisdiction is its ability to make decisions that are not legalistic. As might be expected of a commercial body, the opinions did not contain a comprehensive analysis of the legal cases underpinning their decision. However, at 34 reported pages (including the dissent), the reasons were hardly brief in discussing the basis for the decision.

In light of the precedent the case creates, it is puzzling that the majority made the following statement at the beginning of their decision:

> We do not intend this decision to be a watershed. We do not think that our decision will be tantamount to law reform by setting a precedent that ASIC and future panels will feel bound to follow. Rather, we expect ASIC and future panels to decide whether it is appropriate to give exemptions on the basis of the specific facts in individual future cases.[186]

This statement is not helpful as it attempts to deny the effect that Panel decisions must necessarily have. Given that the majority's decision provided a significant new exemption to the takeover provisions, it is not realistic to declare that this decision does not create a precedent. Indeed, one of the benefits of the Panel reviewing ASIC decisions was considered to be its ability to provide guidance to ASIC through the review process. To achieve this aim, Panel decisions need to contain clear statements of the reasoning adopted (perhaps in the form of guidelines), so that such reasoning can be applied to future ASIC decisions. This does not appear to have been done in this case.

If the creditors of an insolvent company decided in the future that it would be better for them to trade the company out of financial difficulty, perhaps because the market for the company's products was likely to improve in the future, it is foreseeable that they would seek similar relief from ASIC. Unless ASIC could distinguish future applications from the *Pasminco* case, it would be very difficult in practice for it to decline to grant the relief. An analysis of the basis of the Panel's decision makes it difficult to determine the circumstances in which the *Pasminco* situation could be distinguished from future cases.[187]

Subject to the concern that the takeover relief may extend too far into the future, the outcome of the Panel's decision was appropriate in the circumstances. However, the decision does raise two procedural fairness issues.[188] First, it is arguable that there should be an independent assessment of the value of the shareholders' shares. This would test the proposition that the takeover provisions should no longer apply to the shares on the basis that the shareholders would not be paid on a winding up. Second, natural justice concerns arise from the fact that

186 *Pasminco* (2002) 41 ACSR 511, 514 (Byrne P and Lee).

187 See ibid 541 (Micalizzi DP).

188 The rules of procedural fairness apply to the Panel under s 195(4) of the *Australian Securities and Investments Commission Act 2001* (Cth).

the Pasminco shareholders were represented by the directors, who did not have access to the financial information necessary to assess the company's situation.

The *Pasminco* case demonstrates the substantial impact that the Panel can have on our system of corporate regulation. The significance of the takeover relief that may be granted, together with issues concerning the duration of the takeover relief and procedural fairness, reinforce the need to continue to monitor the Panel's progress.