Partial Takeovers

D.M. Gonski* and P.M. Keenan**

I. INTRODUCTION

With the adoption of the Acquisition of Shares Code in each State of Australia and the prior enactment of the Acquisition of Shares Act 1981 (A.C.T.) (the "Code"), there was introduced into the law a mechanism whereby an offeror could seek to gain control of a company without facing any risk of having to proceed to 100% ownership. This facility, the "partial takeover", was a child of compromise. On the one hand was the wish that shareholders in a company should receive offers (for some of their shares at least) whenever possible, and that company directors should be subject to a change in ownership and control even where the potential offeror did not have the resources or the inclination to acquire 100% of the shares on issue. On the other hand was one of the central themes of the Code, namely that upon a change in control of a company each shareholder should share proportionately in the "premium for control" — the additional price incentive which an offeror must typically concede if he is to acquire a controlling block of shares in a company.

This facility for making partial takeover offers under the Code has been increasingly resorted to, both by persons wishing to secure control of a company without paying a full "control premium", and by persons wishing to frustrate a full takeover by absorbing a controlling parcel of shares.[1] This rise in the use of partial takeovers is a cause for some concern. This is so because shareholders faced with a partial takeover must often accept the offers as a matter of choosing the lesser of two evils. Partial offers

* B.Com., LL.B. (N.S.W.), Solicitor of the Supreme Court of New South Wales.

** B.Ec., LL.B.(Hons) (Syd.), Solicitor of the Supreme Court of New South Wales.

1. Recent examples of the use of partial takeovers for each of these purposes include the joint bid in 1984 by Shopping Centres Pty Ltd and Pinna Pty Ltd (subsidiaries of Austram Corporation Ltd) for up to 50.1% of Email Ltd and the bid in 1984 by Cementco Investments Pty Ltd (a subsidiary of Queensland Cement and Lime Company Pty Ltd ("QCL")) for a further 5.1% of North Australian Cement Ltd, so as to take its total holding to 50.8%. In fact the partial bid by Shopping Centres Pty Ltd and Pinna Pty Ltd proved not to be successful.

often present not so much a chance of realising a shareholding on advantageous terms, but a mechanism whereby offeree shareholders are constrained collectively to deliver up control of a company, without any of them receiving the usual (if any) control premium, in respect of the parcel of shares held by them.[2]

The Australian position must be contrasted with that in the United Kingdom where partial offers are generally prohibited and may proceed only with the special permission of the London Panel on Take-overs and Mergers. This permission is granted as a matter of course where the target entitlement is less than 30% or greater than 50%.[3] However, that permission will rarely be granted where the target entitlement is between 30% and 50% — that is, at a level which will potentially leave the offeror in de facto control of the company without requiring it to bid for a majority of the issued capital. Such partial offers are also required by the Panel to be made subject to more than 50% of offerees signifying their approval of the offers on the transfer form to be completed by them. This is quite independent of the decision by each shareholder whether or not to accept the offers with respect to their own shares. Clearly this signification will often require a higher level of approval than the desired level of acceptances of the offers.

The reason why partial takeovers under the Code present shareholders with such a dubious opportunity is the commercial framework in which partial takeover offers fall to be assessed by offeree shareholders. It is trite to say that the price at which full takeover offers will succeed must generally be higher (typically 40% higher) than the price at which that offeror could acquire smaller parcels of those shares. This control premium represents the fact that, depending on the degree of dispersion of shareholdings in the company, a strategic parcel will deliver a disproportionate degree of control of that company. On another view, it is an application of the law of supply and demand, since offers must be pitched at the level of highest shareholder resistance — subject only to compulsory acquisition.[4] Of course, as a corollary, when a partial offeror is able to amass a controlling parcel of shares where no such parcel previously existed, all other

2. See generally B. Bailey and P. Crawford, "The Take-Over Bid by Private Agreement: The Follow-up Offer Obligation" (1983) 7 *Dalhousie L.J.* 94 and the writings there cited.
3. As noted by M.A. Weinberg and M.V. Blank, *Take-overs and Mergers* (4th ed. 1979) 985-992.
4. See discussion of "*Inability to Compulsorily Acquire*" *infra.*

shares will be discounted, given that they have now been stripped of any effective voting power.

Therefore, a shareholder faced with a partial offer is forced to choose between two unsatisfactory results. If control passes to the offeror and he does *not* accept the offer, *all* of his shares will decline in value because:

(a) it is unlikely that further offers will be received for those shares except from the new controlling shareholder (who will in future be bidding from a position of strength), since no other offeror is likely to secure any degree of control of the company unless the new majority shareholder itself accepts; and

(b) some uncertainty is likely to exist as to the future conduct of affairs of the target company. This will be especially so where there is some suspicion that the new majority shareholder will manipulate company policy concerning dividends and other matters so as to cheapen the holdings of minority shareholders. In this regard the weakness of Australian law concerning the oppression of minority shareholders is critical.

If control passes but the shareholder *does* accept the offer with respect to his own shares, the balance of shares held by that shareholder will be discounted as described above; this may well, however, be the lesser of two evils in that a higher price is likely to be secured for at least those shares sold pursuant to acceptance of the partial offers.

Therein lies the 'prisoners dilemma' familiar to economists. The optimum result for each shareholder is often for him to accept the partial offer with respect to his shares, but for other shareholders to reject the offer. However, if all of the shareholders accept the offer, control of the company will pass without any shareholder sharing in a full control premium. Therefore each shareholder is likely to accept the partial offer with respect to his own shares, delivering control of the company to the offeror and stripping the balance of shares held by each offeree of effective voting power.

II. WHAT IS A PARTIAL BID?

Basically, a partial bid is a bid for less than all of the shares of the relevant class in the target.

Partial bids are facilitated by section 16(2)(a) of the Code, which contemplates that offers under a takeover scheme need not be made with the aim of acquiring all issued shares of the relevant class. Section 17, which authorises on-market offers, does not have

this facility and, therefore, a partial takeover can only proceed by way of a takeover scheme.[5]

Partial offers under the Code are of two types. Offers under section 16(2)(a)(i) *relate* to all shares that each offeree holds, but are limited in that the offeror only *proposes to acquire a proportion* of those shares. For example, an offeror might bid for 30% of the issued shares in a company. If *all* shareholders accept, the offeror will acquire 30% from each shareholder and thereby will reach its goal shareholding. If not all shareholders accept, the offeror will take a greater number of shares from each accepting shareholder, so as to achieve its goal shareholding — assuming of course that enough shares are subject to acceptance.[6]

Alternatively, partial offers may be made under section 16(2)(a)(ii) which concerns offers which *relate* only to a *proportion* of the shares which each shareholder holds. For example, an offeror holding 19.9% of the target might bid for 3/8ths of the shares held by each shareholder. Such an offer will only secure 30% of the company if *all* shareholders accept; each rejection will reduce the proportion of shares acquired.

Therefore, offers under section 16(2)(a)(i) relate to all shares in the company in that, by virtue of section 26, where not all shareholders accept the offers those offers can extend so as to embrace a higher fraction of the shares of each offeree who does accept, and thereby achieve the desired shareholding for the offeror. This facility, which does not exist in offers under section 16(2)(a)(ii), has two consequences:

(a) an offeror has the greatest possible chance of achieving its goal shareholding under section 16(2)(a)(i); and
(b) while offerees know the percentage of their shares that they can sell under section 16(2)(a)(ii) offers, they only know the minimum number that they can sell under section 16(2)(a)(i) offers.

Given the general policy of the Code to ensure that control of a company should not pass without each shareholder having an equal opportunity to share equally in any control premium, it is interesting to ask whether partial takeovers which appear to be permitted by section 16 are in fact made illegal pursuant to some other provision of the Code.

No other such provision, however, appears to exist in the Code. Surprisingly, the provisions of section 60 (which relates to

5. The disadvantages of this consequence are considered under "*Takeover Schemes Versus Takeover Announcements*" *infra*.
6. This is achieved through s. 26 which is analysed *infra*.

unacceptable conduct) and provides that the National Companies and Securities Commission ("NCSC") can declare an acquisition of shares (section 60(1)) or "conduct in relation to shares" (section 60(3)) to be "unacceptable", would appear not to apply. This is because sections 60(1) and 60(3) preclude the NCSC from making an adverse declaration except by reference to four stated criteria. These are that the identity of the offeror be disclosed, that shareholders be allowed a reasonable time in which to consider the offers, that shareholders be given sufficient information to assess the merits of the offers, and that all shareholders be given a reasonable and equal opportunity to participate in benefits under the offers. Partial offers made in accordance with the Code will generally satisfy all of these tests. (It has also been suggested that the NCSC might amend the operation of the Code in relation to partial bids pursuant to section 58 of the Code and by reference to the criteria in section 59. Some precedent for this would seem to exist in relation to the deficiency perceived by the NCSC in the operation of section 42 of the Code. This section — the compulsory acquisition section — contains 2 requirements to be met before it can be relied on: that the offeror has become "entitled" to at least 90% of shares of the relevant class (section 42(2)(a)) and that no less than 75% of offerees have accepted the bid (section 42(2)(b)). However, because section 42(2)(b) only applies "if the shares subject to acquisition constitute less than 90% of the shares included in that class" it is possible to avoid this requirement by the offeror holding no more than 9.9% of the relevant shares and 'warehousing' up to a further 10% in an associate. The shares of the associate will be "subject to acquisition" (so that section 42(2)(b) will not apply) and will be part of the 'entitlement' of the offeror. In such a case the NCSC has unilaterally amended the operation of the Code (in reliance on section 58) so as to delete the qualification at the opening of section 42(2)(b). Whether section 58 has a wider regulatory potential is very much at large at this stage.)

In addition, it is interesting to speculate whether, even if section 60 did on its face seem to apply generally to partial bids, the express provision for the making of such offers in section 16 might not override the application of section 60 anyway.

III. ADVANTAGES OF A PARTIAL TAKEOVER FOR AN OFFEROR

1. Acquisition of Control

The principal advantage of partial offers over full offers arises

out of the predicament of shareholders referred to above. Because each shareholder is largely compelled to accept the offers, the takeover gains an aspect of inevitability which increases the pressure on shareholders to accept, and which enables offerors to pitch the offer at a lower price per share than they might otherwise have done. This effect is accentuated by the fact that offers under section 16(2)(a)(i) simply specify an aggregate percentage of shares which the offeror wishes to acquire. If any shareholder does not accept the offer with respect to his shares, the offeror may 'top up' its level of acceptances with shares from other shareholders. Furthermore, because success of a partial offer is often a matter of a change in control of a company, rather than, say, the acquisition of 90% of the shares in a company, the offer price need only appeal to a smaller percentage of shareholders (that is, at a lower level of shareholder resistance) and may be less than the price necessary to attract, say, 90% of the relevant shares.

It has been stated that, at least where no competitive bid emerges, partial offers will often *succeed* at a lesser price per share than would be required for the success of full offers. At the same time, because the offeror stands to gain control of the company without having to purchase all of the shares in that company, it can *afford* to pitch the offers at a higher level than it otherwise could. This is because whatever price is offered by the offeror extends only to the limited proportion of shares which he proposes to acquire. Thus, even if a partial offer is made at a price which includes a control premium, that premium will relate only to a fraction of shares in the company but may well still be sufficient inducement to secure control of the company. Thus, if the bidder already holds 19.9% of the shares in a company, and offers to acquire a further 30% of those shares, even if the offer price includes a fair premium for control, the offeror will gain control while being required to pay a maximum of only 3/8ths of the full control premium of the company.[7]

This leeway is such that in the United Kingdom the London Panel is reluctant to grant its consent so as to allow a partial bid to proceed in competition with a full bid — indeed, if the partial bid is made *before* a full bid, the London Panel will discourage any

---

7. An example of this is the QCL bid for North Australian Cement Ltd, see note 1 *supra*, where QCL offered to purchase only a further 5.1% of shares in North Australian Cement Ltd at $10.00 per share, which succeeded in turning aside the earlier Adsteam bid at $9.00 per share for the 71% of issued shares not already held by it.

extension or revision of the partial bid, and will restrict the partial offeror from dealing.[8]

2. *Cross Shareholdings*

Very often the target company holds shares in the offeror or one of its related companies. Section 36 of the Companies Code is to the effect that a company may not be a "member" of its holding company. The provisions of section 36(5) allow a company which held shares in another company which *later* becomes its holding company to avoid a contravention of section 36 provided it disposes of those shares within twelve months (or such longer period as the court allows) of becoming a subsidiary and does not vote in respect of those shares in the meantime. Often, the need to dispose of cross holdings is a disincentive to making a full bid.

The test of the holding company — subsidiary company relationship is contained in sections 7(1)(b) and 7(4) of the Companies Code, which deem a corporation (X) to be a subsidiary of any other corporation (Y) where:

(a) Y "controls the composition of the Board" of X;
(b) Y controls "more than one-half" of the rights to vote at a general meeting of X; or
(c) Y "holds more than one-half of the issued share capital" of X.

Accordingly, section 36(1) provides that if, for example, X holds 51% of the shares in Y, Y cannot acquire any shares in X and any attempt to do so will be void (section 36(2)). Where, on the other hand, Y already held, say 40% of the shares in X, and X later acquires more than 50% of the shares in Y, section 36(5) provides that Y must dispose of its shares in X within twelve months of becoming a subsidiary of X, and in the meantime Y cannot vote at any general meeting of X.

The advantage of the partial takeover in this case is apparent. If X does hold 40% of the shares in Y, Y may well wish to leave X free to retain that holding and to vote in respect of those shares (since this may provide a good defence for Y against a takeover bid for Y itself). In order to ensure this, Y must proceed by way of a partial takeover for no more than 49.9% of the shares in X, so that X does not become a "subsidiary" of Y and section 36(5) is not triggered. Of course, even if Y does hold less than 50% of X, it still faces the argument that it "controls the composition of the Board", but this is probably a subjective test which is difficult to establish and it is suggested that, without more, a subsidiary relationship is

8. Weinberg and Blank, note 3 *supra*, 998.

unlikely to arise in these circumstances. (One alternative view as to the correct interpretation of the "composition of the board" test is that this test simply looks to the control of more than 50% of voting rights in the election of directors to the board.)

As an aside, it is interesting to note the potentially two-sided nature of the cross-shareholding defence. Assume that X holds 40% of Y and Y holds 49.9% of X as aforesaid. Assume also that a third party, Z, resolves to breach this defensive circle by bidding for the shares in either X or Y (assume that offers are made for shares in X). As soon as Z passes 20% of the issued voting shares in X, section 9(4) of the Code will deem Z to also have a relevant interest in 40% of the shares in Y and (if section 9(4) has a successive operation[9]) Z will immediately be entitled to the 49.9% of shares in X which Y holds. By this means, Z will move from an entitlement of just under 20% of X to an entitlement of 69.9% of X in a single leap for the purposes, *inter alia*, of compulsory acquisition (pursuant to section 42) of the shares of any dissenting minority in X!

It may well be that the deemed entitlement of Z to shares in Y will itself be a breach of section 11, in which case the defensive circle is effective and will require Z to obtain an order by the NCSC under section 58 of the Code relieving it from this consequence. Such an order might well only be made on terms that Z makes "equivalent" offers (whatever that means) for the 60% of Y not already held by X.

However, there will be no consequential breach if, say, shares in X are listed for quotation on the Australian Associated Stock Exchanges (sections 12(k) and 6 of the Code, and Regulation 4) or there are fifteen or less members in Y (section 13(1)). In this case the defensive circle may in fact deliver both X and Y to the aggressor, in that the shares subject to the cross-entitlement are counted for the purposes of establishing rights of compulsory acquisition under section 42 of the Code.

3. *Foreign Investment Limitation*

Where an offeror is a "foreign corporation" or a "foreign person" as defined in section 5(1) of the Foreign Takeovers Act 1975 (Cth), the acquisition of shares by it may fall within the ambit of section 18 of that Act, so as to be subject to an order by the

9. The Exposure Draft released in June, 1984 proposes that the Code be amended to clearly deprive s. 9(4) of successive effect.

Treasurer prohibiting that acquisition if he considers it to be "contrary to the national interest".

An acquisition will fall to be reviewed under the Act where the acquisition would bring the target within the "control" of the foreign offeror (section 18(2)(b)(i)) or, where the target is already controlled by foreign persons not including the foreign offeror, those controllers will henceforth include that foreign offeror (section 18(2)(b)(ii)). Such a "controlling interest" is deemed to exist where:

(a) a foreign corporation or person (together with any associate) controls 15% or more of voting power or holds 15% or more of issued shares; or

(b) two or more foreign corporations or persons (together with any associate of either of them) control 40% or more of voting power or hold 40% or more of issued shares.

An offeror proceeding by way of a full takeover offer will, if successful, gain the level of control which triggers section 18 of the Act so as to be subject to an adverse order by the Treasurer. Partial offers however, which limit the greatest potential number of shares to be acquired by a foreign offeror to, say, 14.9%, will avoid this liability.

Alternatively, a foreign offeror might obtain the permission of the Treasurer to acquire shares in an Australian target up to a certain maximum level, often less than 50%. Clearly, only a partial takeover will enable the foreign offeror to acquire shares up to this permitted level while ensuring that the ceiling is not exceeded.[10]

4. *Trade Practices Act*

Section 50(1) of the Trade Practices Act 1974 (Cth) as presently drafted prohibits the acquisition by any corporation of any shares in a body corporate if, as a result, the acquirer "would be, or would be likely to be, in a position to control or dominate a [substantial] market for goods or services [in Australia]", or would "substantially strengthen" such a position where it already exists.

Section 50(2) deems a corporation to be in such a position if two or more "related" bodies corporate are together in such a position.

---

10. An example of such a bid are the offers in January, 1982 which secured for Nationale Nederlanden (Aust.) Ltd 49.9% of the issued shares in Mercantile Mutual Holdings Ltd. Similarly, in the course of the Austram Group bid referred to in note 1 *supra* White Consolidated Industries Ltd of the United States announced an intention to seek permission of the Treasurer to lift its holdings in Email Ltd from 14.9% to just under 20%; this permission was later granted.

Sections 4A(1) and (5) have the effect that bodies corporate will be "related" in circumstances very close to those which give this result under section 7 of the Companies Code. That is, corporations will be related where one is the holding corporation of the other, or where both corporations share the same holding corporation.

These provisions together suggest a critical advantage obtainable under partial takeover offers where the offeror might otherwise face arguments of "dominance or control" under section 50. Partial offers which have a ceiling on acquisition at the 49.9% level will not trigger the deeming provision in section 50(2) unless the offeror gains control of the composition of the board of the target at less than 50%. However, as noted above, control of the composition of a board of directors is clearly a less readily identifiable basis for regarding corporations as "related", and is more difficult to prove. Therefore, an offeror who acquires marginally less than 50% of the issued shares of its target might well achieve its strategic ambitions without being regarded as related to the target.

If this is so, the acquisition might only be attacked under section 50 without the benefit of section 50(2), and so it must be proved that the offeror *itself* is in a position to control or dominate the relevant market. Such a breach can only rely on the de facto control or dominance through the target company to the extent that this can be independently proved.

It should finally be noted that the draft amendments to section 50 now before Parliament will remove the deeming provision that now exists in section 50(2).

5. *Retention of Listing*

In order to maintain listing for quotations on the Australian Associated Stock Exchanges it is necessary for a company to have a "sufficient spread" of shareholdings (Listing Requirement 3J(9) and see Listing Requirement 1(3)), which is generally interpreted to mean that not more than 75% of shares in the company may be held by one shareholder and that there must be at least 300 shareholders in total.

A full takeover offer may jeopardise this listing by eroding the sufficient spread, in which case the listed company is likely to be given three months in which to return to a satisfactory shareholding spread.

Partial (as opposed to full) takeover offers will often avoid this problem and its attendant risks by making it more likely that a sufficient spread of shares is at all times maintained, depending on

the proportion of shares proposed to be acquired. (At least the number of shareholders will not change as a result of a partial takeover under section 16(2)(a)(ii) or a takeover under section 16(2)(a)(i) in which the number of shares subject to acceptance exceeds the number of shares proposed to be acquired.)

There have been many situations recently where "back-door listings" have been acquired by the takeover of "listed shells". It is interesting that none of these takeovers have been done by way of partial bids, the bidders in each of these cases having taken the risk of the bids being too successful. It is suggested that the reason for the reluctance to use the partial bid is the assumption that a higher price per share will have to be paid under that bid than under a full bid. As noted above, this assumption is probably incorrect. There seems no legal reason why the partial bid should not be preferred.

6. *Accounting and Taxation Advantages*

Section 269(3) of the Companies Code requires that a holding company shall cause consolidated group accounts with respect to itself and each of its subsidiaries to be prepared. Section 7(1) defines subsidiary (in the manner referred to above) primarily by reference to the holding of shares in that company, and once again in general terms the test is whether or not more than 50% of shares are held in any given company.

Therefore, where a target company has substantial accumulated losses, the offeror may wish to avoid having to introduce those losses into the consolidated group accounts. This can be achieved by the offeror proceeding by way of a partial takeover where the proportion of shares which it proposes to acquire will not give it more than 50% of the issued shares in the company so as to render that company a subsidiary.

This aspect goes further in that subsidiary status has a number of ramifications under the Income Tax Assessment Act 1936 (Cth) (the "ITAA"). Section 80(2) of the ITAA, which provides for a seven year carry forward of tax losses so as to preserve deductions until sufficient income is generated to make use of them, is predicated upon a substantial continuity of either beneficial ownership or the business of the company in the relevant period. Section 80A(1) of the ITAA contains the beneficial ownership of shares test, which requires that shares carrying between them rights to more than 50% of voting power, dividends and return of capital, "were beneficially owned by persons who, at all times during the year in which the loss was incurred, beneficially owned

shares in the company carrying between them rights of those kinds."

Clearly, there can be no guarantee that this test will be satisfied where control of the company changes hands pursuant to a takeover, if the takeover offers are for up to 100% of the target company. In contrast, partial takeover offers which relate to less than 50% of the shares in the target (and perhaps comfortably less, say, 40-45%) will give this result in that no previous shareholder will be able to quit the company altogether (unless the bid is made pursuant to section 16(2)(a)(i) and the level of acceptances is low) so that, prima facie, there will be no loss in shareholders. Where the company is not a private company for income tax purposes, section 80A(1)(b) provides that such a carry forward of losses will exist where the Commissioner considers it reasonable to assume that the criterion set out above is satisfied. Once again, it is strongly arguable that it is reasonable so to assume where the offeror has merely acquired, say, 40% of shares from each pre-existing shareholder. Where the target is a private company for income tax purposes, the Commissioner must be satisfied that the criterion above has been met (section 80A(1)(a)).

However, a partial takeover may also be of more general assistance under the ITAA in that the definition of "private company" in section 103A of that Act is such that a partial takeover designed to leave 50% or more of issued shares in the hands of the public is likely to preserve the status of a company as a public company for income tax purposes even where the offeror is a private company for those purposes.

7. *Avoidance of Mandatory Offers*

A partial takeover avoids the limited provisions in the Code that compel a full takeover offeror who has become entitled to 90% of the relevant shares to make offers also to acquire all shares of the target of a class different to that to which the takeover offers related.

Previously the stock exchange listing requirements contained comprehensive provisions requiring an offeror who was bidding for all of the shares in a class of shares in a company to make offers also for shares of other classes in the company. Now this requirement exists only in a diluted form in section 43(4) of the Code, which requires an offeror who has become entitled to 90% or more of the voting shares in a company during an offer period to give notice to the holders of all non-voting shares, renounceable options or convertible notes to which it is not entitled. These

holders may then, within three months after the giving of the notice, require the offeror to acquire the shares, options or notes held by them (section 43(6)).

A partial takeover will seldom cause the offeror to become entitled to 90% or more of voting shares in the company, and therefore will avoid the requirement in section 43(4). This could be a great advantage if, for example, the other shares issued in the company include preference shares at a rate of dividend advantageous to the company.

8. Other Specialised Legislation

It has been seen above that the avoidance of a holding of more than 50% of shares in a target may well have considerable advantages under various key pieces of legislation. These advantages also exist under more specialised pieces of legislation such as the Broadcasting and Television Act 1942 (Cth) (under this heading referred to as the "Act").

Part IV Division 2 of the Act deals with the holding of interests in radio station licences. Section 90C of the Act prohibits a person holding a "prescribed interest" in *inter alia* more than one metropolitan commercial radio station in any State or more than four metropolitan commercial radio stations in Australia. Sections 90(2) and (3) define a prescribed interest as being the holding of a licence, "control" of a licence (defined in sections 90D and 90E) or the holding of a "shareholding interest" (that is, a beneficial interest) in shares representing more than 15% of paid-up capital in a company which is a licence holder.

At first glance, this provision appears to preclude any relevance of the Code at all, since the 15% limitation is below the 20% threshold in the Code. However, section 90B provides for the tracing of shareholding interests through successive companies, with the result that the partial takeover might be the only way of securing control of a company 'upstream' of the licence holder, without falling within the ambit of the Act. For example, assume that A holds a metropolitan commercial radio licence, that B holds 50% of the shares in A, and that C holds 50% of the shares in B. Section 90B will deem C to have a shareholding interest of 25% in A, the licence holder. Assume also that X wishes to acquire control of C, but that X already has a prescribed interest in another commercial radio licence in the same metropolitan area. Because 90B(2) makes it clear that the section operates successively (contrast section 9(4) of the Code, discussed above), X will be deemed to have a "prescribed interest" in the radio

licence held by A and so will be in breach of section 90C(1)(a) if it acquires a shareholding interest greater than 60% in C. At this point the importance of the partial takeover becomes obvious: an offer for more than 60% of C runs the risk of entangling the offeror in the intricate web of the Act.

Parallel provisions exist in relation to commercial television stations in Part IV Division 3 of the Act. In this case, the central limitation is set out in section 92(1) which again refers to the concept of a "prescribed interest". This term is defined in section 91(2), again by reference to the holding of a licence or "control" of a licence (defined in sections 92A and 92B), but also *inter alia* by reference to "shareholding interests" exceeding 5% (rather than 15%) of total paid up capital. Section 91A contains the provisions for tracing a shareholding interest.

For completeness, it is noted that section 90F (concerning radio station licences) and section 92C (concerning television station licences) contain similar limitations on directors of "two or more companies that are, between them, in a position to exercise control of" certain combinations of licences. In both cases, "control of a licence" is defined (sections 90D and 92A respectively) to include "control of a company" which is in turn defined (sections 90E and 92B respectively) by reference to various shareholding interests in a licence holder.

As well, sections 90G and 92D contain additional limitations where "foreign persons" are concerned. The partial takeover may be critical in dealing with any of these provisions.

Alternatively, an offeror might acquire such a level of shares in a company as to involve it in a *prima facie* breach of section 90C or section 92(1), but instead rely on the notice procedures contained in sections 90J and 92F which in certain circumstances entitle a person who would otherwise be in breach of section 90C or section 92(1) to hold prescribed interests in contravention of those sections without being in breach of the Act for up to six months or such longer period as the Australian Broadcasting Tribunal ("ABT") allows, (sections 90C(5B)(c) and 92(4B)(c)).

Therefore, an offeror might either avoid the Act altogether by use of the partial takeover, or proceed by way of a full takeover and be in temporary contravention of the Act, but remedy this contravention by selling shares so as to reduce its number of "prescribed interests" down to the permitted level within the

periods of grace which follow upon the giving of notice to the ABT as referred to above.[11]

9. *Trust Deed Ratios*

Commitments entered into by an offeror will often reproduce the 50% shareholding tests referred to above. Typically, older debenture trust deeds and the like will provide that the liabilities of a target company are to be taken into account in determining compliance with trust deed ratios when that company becomes a subsidiary as defined in the Companies Code. However, those same documents often provide that the assets of such a new acquisition are to be disregarded unless and until the offeror proceeds to acquire 100% of the shares in the target. Accordingly, for a period (that is, while the offeror moves between 50% and 100% of the target) the offeror will be in breach of the ratios with consequential ramifications.

The newer deeds accept that such a breach may occur and give the relevant company three months in which to remedy that breach, either by rescinding contracts arising from acceptances of its offers or by compulsorily acquiring the shares of any dissenting minority so as to make the target a wholly owned subsidiary. Clearly therefore, offers by such a company must be made by way of a takeover scheme and must be conditional upon fulfilment of the preconditions necessary for the offeror to proceed to compulsory acquisition.

This position is avoided under a full takeover scheme by inserting in the offers a minimum acceptance condition sufficient to ensure that contracts arising from acceptances of the offers may be rescinded *ab initio* unless the offeror becomes entitled to compulsorily acquire outstanding shares under section 42 of the Code. Of course, such rescission will spell the failure of the bid.

The position might also be avoided by simply proceeding by way of partial takeover offers where the proportion of shares in the target which the offeror proposes to acquire are insufficient to render that target a subsidiary of the offeror. In this case the liabilities of the target will not be taken into account under the offeror's trust deeds in the first place, while at the same time the offeror may well gain *de facto* control of the target.

---

11. An illustration of the latter technique is the sale in June, 1984 by The North Queensland Newspaper Company Ltd ("NQN") of approximately 10% of the shares in Rockhampton Television Ltd, thereby relieving the holding company of NQN, News Corporation Ltd, of a contravention of s. 92(1) of the Act.

A further possible difficulty of this nature exists where the *target* has a trust deed which will require that an offeror which becomes its holding company must guarantee the obligations of the target under the trust deed. Such a guarantee might involve some legal or commercial problem for the offeror, for example if it would be the offeror in breach of a trust deed limitation on its external liabilities. A partial bid which avoids any holding company — subsidiary relationship from arising might be the only way of avoiding such an outcome.

IV. DISADVANTAGES OF PARTIAL TAKEOVERS

1. *Financial Assistance*

It is not uncommon for an offeror to defray the costs of a successful takeover by recourse to the financial resources of the newly acquired wholly owned subsidiary. It is true that such an action is *prima facie* a breach of section 129(1) of the Companies Code, which prohibits the giving by a company of financial assistance for the acquisition of shares in that company by any other person. However, a successful offeror will typically rely on section 129(8)(a) which excludes from the operation of section 129(1), "the payment of a dividend by a company in good faith and in the ordinary course of commercial dealing". This provision has been construed as giving shareholders a veritable carte blanche in the payment of dividends by newly acquired subsidiaries. This is so partially because the qualification in section 129(8)(a) that the dividend must be paid "in good faith" and "in the ordinary course of commercial dealing" appears to be an irrelevant limitation, since a payment of dividend would seem to be a domestic matter between the company and its shareholders and therefore to be outside the range of any "commercial dealings". Further, to the extent that the payment of dividends can be regarded as constituting a "commercial dealing", it is (on one view) difficult to conceive of the "ordinary course" of those dealings without including within it dividends of almost any size paid in almost any circumstances.

As well, section 129(8)(k) preserves the general law exceptions to section 129(1) which (arguably) include the proposition that, "the payment of an ordinary revenue dividend is part of the normal functions of the company, and one feels that it ought to be justified whatever the company's purpose in declaring and

paying it".[12] Therefore, section 129(1) is an imperfect barrier to the reduction of the effective price of a takeover by drawing on the resources of the target.

It is otherwise, however, where the offeror made only partial takeover offers and holds only, for example, 50% of the issued shares in the target. This is so because:

(a) where the target is 100% owned, financial assistance which reduces the effective cost of the acquisition to the offeror causes no more than a dollar-for-dollar reduction in the value of the target. Where the target is only partially owned, and assuming that the financial assistance takes a form available to all shareholders (e.g., payment of a dividend — whether or not this is "financial assistance" for the purpose of section 129), such financial assistance causes a reduction of the assets of the target greater than the reduction of effective cost of the acquisition to the acquirer; the difference between these amounts is the extent of the "leakage" of assets of the target to the remaining minority shareholders;

(b) should it be determined to proceed by way of special resolution under section 129(10) in the giving of financial assistance to the offeror, the minority shareholders may well block the necessary resolution unless those shareholders will benefit equally from the proposed use of resources of the target. This is particularly so if they remain embittered at the transfer of control of the company at an inadequate offer price; and

(c) whatever action might be taken, the new controlling shareholder is open to allegations of breach of section 129 (even if he relies on the dividend exception) or of oppression of and fraud on the minority. Additional actions might well lie against the directors of the newly acquired subsidiary. (See *3. Dissenting Minorities* below.)

Quite apart from the limitations of a partial bid in reducing the costs of the acquisition to the offeror, the new group may well have only a limited capacity to borrow on the strength of consolidated balance sheets where the target is not made a wholly owned subsidiary.[13]

---

12. *Re Wellington Publishing* [1973] 1 N.Z.L.R. 133, 136 *per* Quillam J. This *dictum* is not universally accepted, however, where the dividend is not declared out of revenue profits.
13. J.G. Williams, *Acquisitions and Mergers* (1980).

2. *Inability to Compulsorily Acquire*

Section 42 of the Code enables an offeror, in certain circumstances, to compulsorily acquire the shares of a minority of dissenting shareholders, so as to make the target a wholly owned subsidiary of the offeror. This will be available where the offeror has become entitled, during the offer period, to 90% or more of the shares of the relevant class not already held by the offeror.[14] Where the offeror already held 10% or more of those shares before the offer period commenced, it must also receive acceptance from at least 75% of offeree shareholders. This facility is not available unless the offeror "proposes to acquire all the shares included in [the relevant] class",[15] and therefore a partial takeover will never entitle an offeror to compulsorily acquire the shares of a dissenting minority.

3. *Dissenting Minorities*

A partial offer by definition will leave a minority of shareholders to which the company and its directors will remain accountable. This minority may well feel that control of the company was taken on terms disadvantageous to them. It will often also include persons who used to be the major shareholders in the company and who still retain significant parcels.

Such a minority may restrict the activities of the company and pose the threat of fraud on the minority actions against the offeror or breach of directors' duties actions against the directors of the target (who cannot sublimate the interests of the target to those of the group as a whole).[16]

The minority may well also add considerably to the administrative costs of running the company. They will be entitled to receive properly audited accounts and to have those accounts presented to an annual general meeting held each year. In addition, they will be entitled to requisition meetings under section 241 of the Companies Code, to take legal action for perceived frauds on a minority or oppression, and to combine so as to represent a voting block able to frustrate the intentions of the controlling shareholder.

4. *Inability to Buy on the Market*

A bidder can generally only acquire shares on the market where:

---

14. S. 42(2)(a).
15. S. 42(1)(a).
16. *Reid Murray Holdings Ltd (In Liq.)* v. *David Murray Holdings Pty Ltd* [1972] 5 S.A.S.R. 386.

(i) such acquisition will not lift its entitlement beyond the 20% threshold in section 11;

(ii) it has made a takeover announcement pursuant to section 17 of the Code; or

(iii) it has served on the target company a Part A Statement and the offers to be despatched pursuant to that Statement:

(a) contain no conditions other than a minimum acceptance condition and conditions requiring the non-occurrence of any "prescribed occurrence" as defined in the Code; and

(b) propose that the offeror acquire up to all of the shares in the target not already held by it,[17]

provided in (ii) and (iii) above that such an acquisition is not in breach of section 40 of the Code.

By virtue of (iii)(b) above, therefore, there is a distinct advantage, where the target is a listed company, in proceeding by way of a full takeover. This advantage will be lost where listing of shares in the target is suspended.[18]

As will be seen, partial takeovers must proceed by way of a takeover scheme which, as noted above, can never be a "relevant takeover scheme" for the purposes of section 13(3)(b). Such a scheme will, therefore, avoid the strictures of section 11 only in accordance with section 16(2)(d) of the Code, which imposes a two week period immediately following service of the Part A Statement in which the offeror cannot acquire any shares in the target beyond the 20% threshold in section 11.

Partial takeovers do not allow buying past the 20% limit in the fourteen days following service of the Part A Statement. This can be critical given the speed with which takeover battles can be won and lost.[19]

5. *Takeover Schemes Versus Takeover Announcements*

The inability to mount partial offers by way of on-market offers in accordance with section 17 of the Code is a significant loss to an offeror. It will face the following relative disadvantages:

(a) Sections 16(2)(d)(i)(B) and 18(1) of the Code require that a Part A Statement may not be served until registered with the NCSC, through its delegates the Corporate Affairs

17. S. 13(3).

18. This occurred in the takeover of Datronics Corporation Ltd by Central Management and Finance Ltd and John Foster Valley Ltd in May, 1984.

19. The on-market takeover by Australian National Industries Ltd for Comeng Engineering Ltd, for example, secured control of the target within two days of the on-market announcement.

Commission ("CAC") in each State and Territory, while section 18(2) gives the NCSC wide and subjective terms of reference in determining whether or not to register such a Part A Statement. By contrast, section 17(10)(a)(iii) merely requires that a copy of a Part C Statement be 'lodged' with the CAC. Although the practice has emerged of voluntarily submitting Part C Statements to the scrutiny of the CAC, this is not mandatory and could be dispensed with, giving the on-market offeror a time advantage of at least several business days. Clearly, if the on-market price is right, control might pass while the Part A Statement is still under discussion with the CAC.

(b) Similarly, any variation under a takeover scheme (including an increase in price) must be effected in accordance with section 27(10) of the Code, which again involves registration of the notice of variation with the CAC[20] and the printing and dispatch to each offeree of a copy of the notice of variation as registered. While registration of such notices is typically a matter of formality and incurs little delay, the printing and dispatch of those notices is more time consuming. By contrast, the price of an on-market announcement is increased by simply acquiring shares at the higher price.[21]

(c) The price flow-on or escalation provision concerning takeover schemes[22] is both retrospective and prospective during the offer period, so that even offerees who accepted the offers prior to any price increase (or substitution of alternative consideration) can elect to take that higher price (or alternative consideration) instead of the initial offer price. The escalation related to on-market offers[23] is not retrospective. Only offerees who subsequently accept will receive the higher price. This means that an on-market offeror has greater flexibility to increase its price so as to win over resisting shareholders. By the same token, it might be expected that increasingly sophisticated offerees will wait until the last 5 days of an on-market offer period so as not to miss out on any price increase.[24]

(d) An offeror under a takeover scheme may be compelled to delay printing of the offer documents and Part A Statement

20. S. 27(13).
21. S. 17(8).
22. S. 31.
23. S. 17(8).
24. S. 17(9).

until receipt of the Part B Statement from the target company, since section 16(2)(f)(viii) requires the offeror to send copies of the Part B Statement with its own documents in certain circumstances. By contrast, the Part D Statement given by the target in response to a Part C Statement related to on-market offers is simply lodged with the home exchange of the target[25] and with the CAC. It does not, therefore, impinge upon dispatch of the Part C Statement, again giving the on-market offeror a significant advantage in timing and flexibility.

(e) In cases where the offeror is a natural person who is a director of the target, or where any person is a director of both the offeror and the target, section 23 will require the Part B Statement given by the target board to include an expert's report stating "whether, in his opinion, the takeover offers are fair and reasonable and stating his reasons for forming that opinion." This requirement does not exist where the offeror has proceeded by way of on-market offers. Note, although an expert's report is also required where the offeror already holds 30% or more of shares in the target, such a bid cannot be made on-market without the consent of the NCSC,[26] and therefore the on-market bid is not a generally available alternative in this situation.

6. *Vulnerability to a Full Bid*

It is the major thrust of this paper that a partial offeror will, all other things being equal, have greater flexibility than a full offeror in setting the offer price. However, it remains the case that a full offeror with greater cash resources and/or greater determination to win the target company will make commercially superior offers if it offers at the same (or even a slightly lower) price to that offered under the partial offers. This follows from the discount of shares held by each offeree if control of the company passes to the partial offeror. Therefore, it is possible that a partial bid will lose to a full bid at the same or even a slightly lower price. Of course, at any comparable price per share the expense to the offeror making the full bid is potentially far greater than that of the offeror making the partial bid.

7. *Risk of not Achieving Control*

In a full bid there is the risk that the offeror will not get

25. S. 32(1).
26. S. 17(3).

sufficient acceptances to compulsorily acquire the remainder. In a partial bid there are two risks: firstly that the offeror has not chosen a proposed shareholding level sufficiently large to secure control of the target; and, secondly, as with the full bid, that there will not be enough acceptances of the offers to give control. The question of the minimum level of shareholding which will secure control may be problematical since:

(i) the minimum shareholding level which will give control depends (inter alia) upon the degree of dispersion of remaining shares in the company; if those shares prove to be less widely held than believed, the parcel of shares acquired by the offeror may not carry control; and

(ii) the target may place further shares with selected 'friendly' parties so as to dilute the shareholding acquired by the offeror.[27]

Of course, in both a full and a partial bid the risk of not achieving sufficient acceptances may be minimised by imposing a minimum acceptance condition at a level thought to imply control. Thus, an offeror might think that a parcel of 30% will give him voting control of a company and will frame his partial offers accordingly. However, it might well reach this level without gaining control if the offeror has miscalculated the dispersion of shares in the company or if a new voting block were to emerge, whether as a result of the advent of a new offeror or of the co-operation between existing shareholders. Of course, if such co-operation relates to more than 20% of the voting shares it must not amount to an 'acquisition of shares' as defined in sections 7(1) and 8(7) together with the creation of an 'association' as defined in section 7(4), or else such co-operation will itself be in breach of the central prohibition in section 11.

Where a partial offeror fails to achieve the control sought by virtue of an allotment of additional shares in the target company, that offeror will be entitled to withdraw his offers if they contain a condition that no "prescribed occurrence" should take place in relation to the target company in the relevant period.[28] Although the right to withdraw contained in section 21(1) is limited so as not to arise within the first fourteen days after dispatch of the offers, the failure of such a condition will entitle the offeror to rescind *ab initio* any contracts arising from the offers. In this second case,

---

27. This occurred in the facts examined in *Scott* v. *H.S. Lawrence & Son Pty Ltd* [1982] 1 A.C.L.C. 238.
28. See s. 6 of the Code.

the directors of the target company may well face the argument that they have breached their duties to the company.[29]

V. AREAS OF CONTROVERSY

1. All or nothing offers?

The difference between offers under section 16(2)(a)(i) and offers under section 16(2)(ii) has been analysed above. It is interesting to speculate whether offers made under either of those provisions might be drafted so as to be capable of acceptance in part, as well as to acceptance for the full ambit of the offers. Thus, an offer under section 16(2)(ii) might relate to 50% of the shares of each offeree, or such lesser percentage of the shares of each offeree which he is prepared to sell under the offers. There is even greater scope for this under section 16(2)(a)(i) offers where the offeror might propose to acquire up to 50% of the shares in the target, but the offer to each individual shareholder might be open to acceptance in respect of that number of shares of each offeree determined in accordance with section 26 (see below) or such lesser number as each offeree might signify in writing on the form of acceptance and transfer.

This possibility would seem not be be precluded by the Code; in particular:

(a) while section 16(2)(a)(i) requires the offeror to specify the proportion of shares in the target proposed to be acquired, nowhere is it required to specify the minimum number of shares with respect to which any individual offeree may accept the offers; and

(b) section 26, in referring only to "acceptances of the take-over offers"[30] leaves open a possibility that, although the offers *relate* to all shares of each offeree, they may be *accepted* as to part of that holding. This implication is continued in section 26(2) which deems each acceptance to relate to a certain proportion of shares held by each offeree, *but only by reference to the "available number of shares"* as defined in section 26(1)(b)!

---

29. This was the case in *Howard Smith Ltd* v. *Ampol Petroleum Ltd* [1974] A.C. 821. However the rule established by that case has now been eroded by the decisions in *Cayne* v. *Global Natural Resources P.L.C.* (Chancery Division, 12 August, 1982, unreported but referred to in (1982) 56 *A.L.J.* 600) and *Pine Vale Investments Ltd* v. *McDonnell and East Ltd* [1983] 1 A.C.L.C. 1294.

30. S. 26(1)(b).

As a matter of policy under the Code, and section 60 in particular, this aspect of the offers should not engender uncertainty and no doubt the offers would provide that, unless an accepting offeree signified a contrary desire, the maximum possible percentage of his shares (in accordance with section 26) would be acquired. Therefore, this possibility would seem to be a matter of drafting rather than of law.

This mechanism might elicit a greater level of acceptance by giving offerees a greater choice. Of course, by the same token, those offerees who might otherwise have felt constrained to accept the offers with respect to *all* their shares, may now only accept in part. The net effect must be a matter of commercial judgement in each case.

2. *Section 26*

Section 26 of the Code, which is critical to the operation of section 16(2)(a)(i) offers, concerns the pro-rating of offers and of acceptances in cases where the total number of shares subject to acceptances of the offers (referred to in section 26(1) as the "available number of shares") exceeds the number of shares which the offeror proposed to acquire under the scheme (referred to in the sub-section as the "desired number of shares").

Section 26(2) provides that, where the available number of shares exceeds the desired number of shares, the offers shall be deemed to relate only to (and to have been accepted only as to) that proportion of shares held by each offeree that is equal to the proportion of the desired number of shares to the available number of shares. That is to say, where acceptances exceed the target number of shares, the offers and the acceptances of those offers are deemed to abate proportionately, so that each shareholder will sell pursuant to the offers an equal percentage of shares held by him, being the percentage which gives the offeror the desired number of shares.

For example, assume that an offeror proposes to acquire 30% of the shares in the target, and that it already holds 19.9% of those shares. If acceptances under the partial offers amount to 30% or less of issued shares, the offeror will acquire all shares of each accepting offeree. If all offers are accepted, that is, acceptances relate to 81.1% of shares not already held by the offeror, the offeror will acquire slightly less than 3/8ths of the shares of each offeree. At points in between these extremes, it will acquire between 100% (assuming insufficient acceptances) and 37.5% (assuming total acceptance) of the shares of each offeree.

As noted above, this mechanism boosts the 'inevitability' of the takeover, increasing the pressure on each offeree to accept and reducing the level of any control premium necessary for success.

However, section 26 is drafted in such a way as to have a further consequence adverse to the interests of shareholders in the target[31] and, potentially, of the offeror. This is the fact that section 26, in calculating the pro-rating of offers and acceptances in cases of an 'over-subscription', refers (in section 26(1)(b)) to "acceptances of take-over offers". This phrase clearly excludes shares acquired outside the takeover scheme, whether by reliance on section 11 (which permits any acquisition of shares until the acquirer has reached the 20% threshold) or any other exception to section 11. Possibly, section 26 was drafted in this fashion so as to ensure that offerees are certain of being able to accept the offers at least as to a minimum percentage of their shareholding. Were section 26 drafted so that the desired number of shares was reduced by the amount of any shares acquired outside the takeover scheme, offerees would be deprived of even this element of certainty. At the same time, this drafting also has the effect that an offeror must be careful in purchasing shares outside a partial takeover scheme to remain within the limitations on his ability to finance the total purchase price (remembering that it must still be able to acquire under the scheme the proportion of shares proposed to be acquired by it under the scheme).

This difficulty faced by offerors cannot be removed by appropriate drafting of the statement of the proportion of shares proposed to be acquired under the takeover scheme pursuant to section 16(2)(a)(i). It is the view of the writers that it is not possible to comply with section 16(2)(a)(i) while avoiding the difficulty referred to above, since any accommodation for shares acquired *outside* the scheme must leave any statement in purported compliance with section 16(2)(a)(i) insufficiently certain to gain registration.[32]

A further potential for abuse of section 26 by offeree shareholders to the detriment of the offeror exists where the target company is listed. This flows from section 26(3) which provides that, where the offeree would be left with an "odd lot" after sale of his shares by way of acceptance of partial offers, the offeror must also acquire that odd lot. While an odd lot is not defined,

31. D. Gross, "Partial Takeovers — A Critique of the Provisions in the Companies (Acquisition) of Shares Act and Codes" (1983) 1 *Company and Securities L.J.* 251, 258-260.

32. See the wide discretions given to the NCSC by s. 18.

section 6 defines a "marketable parcel" (which is also referred to in section 26(3)) by reference to the business rules of the home exchange of the target. For example, the listing requirements of the Australian Associated Stock Exchanges define a marketable parcel as a parcel of shares with an aggregate market value which depends on the price of each share but which in all cases represents a total price of $100 or greater.

Since section 25 deems offers under the Code to extend to persons who become registered or entitled to become registered *after* the commencement of the offer period, there is nothing to prevent an offeree from splitting his shareholding into odd lots and transferring those to various associated entities. Taken to its limit, such a share split would convert partial offers into full offers!

We consider that section 26(3) ought to be amended to close this possibility, which has two potential repercussions:

(a) it may involve the offeror in expenditure beyond its means, rendering useless the requirement of paragraph 3 of Part A of the Schedule to the Code that the offeror state the manner in which it intends to satisfy its obligations to accepting offerees; and/or

(b) it may cause the offeror to withdraw under section 21. In addition, NCSC Policy Statement No. 107 suggests that the NCSC would favourably consider offers conditional on not more than a stated percentage of shares in the target being acquired pursuant to section 26(3).[33]

Effective amendment of section 26(3) might easily be done by providing that the offeror need only acquire those odd lots which existed *prior* to the first announcement of the offers. Once again, the authors doubt that any specification in the Part A Statement itself of the shares to be acquired which might prevent this abuse would be in accordance with section 16(2)(a)(i).

A further weakness of section 26 is that section 16(2)(f)(vii)(A) requires offers not subject to a "prescribed condition" to state that accepting offerees will receive the relevant consideration within thirty days after acceptance. Yet, if the offer is extended beyond the minimum period of one month,[34] the offers and acceptances will not have been pro-rated under section 26 before the date for payment. This can be avoided by the offeror inserting

---

33. Policy Statement No.107 primarily concerns ss 13(3) and 13(4) of the Code, but the views stated therein can probably be adapted to this context.
34. S. 16(2)(f)(ii).

into the offers a prescribed condition which is not waived so that section 16(2)(f)(vii)(B) will extend the period for payment until thirty days after the offers become unconditional. Alternatively, this problem can be remedied by an order by the NCSC given pursuant to section 58 and similar to that referred to below.

3. *Conversion of a Partial Bid into a Full Bid*

The advantages and disadvantages of the partial takeover, as against the full takeover, are canvassed above. These differences suggest the further question whether one can have ones cake and eat it, by varying partial offers so as to change them into full offers. This might be appropriate where, for instance, an offeror has revised its estimates of the worth of the target and now wishes to acquire all of the shares in the target (hoping no doubt to be able to rely on section 42 to achieve this).[35]

Variations of offers under a takeover scheme are governed by section 27, which provides that offers may only be varied in accordance with section 27 or with the consent in writing of the NCSC. However, as section 27 refers in detail only to a variation to the consideration offered, or to the offer period, the question whether offers can be converted from partial into full offers becomes a matter of gaining the acceptance of the NCSC, without any provision of the Code being expressly relevant to the question.

In favour of such a variation, it is arguable that:

(a) for the NCSC to refuse a variation under section 27 simply necessitates the commencement of a new scheme (or takeover announcement) which serves only to delay the offeror, not to prevent it following its desired path; and

(b) since offers under a takeover scheme may be withdrawn after the fourteen day period following dispatch of the offers[36] permission for the variation proposed might be the only alternative to the loss, by shareholders who have not yet accepted the offers, of any opportunity to sell their shares to the offeror,[37] unless in fact the offeror withdraws the partial offers and makes full offers as proposed in the first place.

---

35. Such a conversion has in fact already been effected in January, 1984 by I.E.L. (Tasmania) Pty Ltd (a subsidiary of Industrial Equity Ltd) when it converted a partial bid for approximately 40% of the shares not already held by it (namely 11.7%) in the Cascade Brewery Company Ltd into a full bid for that company. However, in that case no attempt was made to compulsorily acquire the balance of shares in the target pursuant to s. 42.
36. S. 21(1).
37. S. 21(2)(a).

Complete withdrawal could be effected by rescission of contracts that had already arisen pursuant to an appropriately worded prescribed condition.

It may be however, notwithstanding the precedent above,[38] that the permission of the NCSC under section 27 may not be enough, and that such permission would have to be accompanied by an order under section 58 of the Code varying the operation of the Code so as to excuse the offeror from having a Part A Statement which no longer properly reflects the offers (note that section 27 does not provide for consequential amendments to the Part A Statement).[39]

4. Combination of a Partial Takeover with a Full Takeover

A partial takeover which succeeds in delivering control of a company to the offeror may then be followed, once it has closed, by a full takeover for the remainder of the shares. This technique has the potential advantage to the offeror of taking its shareholding in the company above 90% so as to enable it to compulsorily acquire the remainder, and thus render the company a wholly owned subsidiary *without* having at any stage to make a full takeover at a price which includes a control premium. (Admittedly, an offeror proceeding in this manner must also receive acceptance to its full offer by at least 75% of offerees so as to proceed under section 42.)

It has also now become a recognised practice to make offers under a takeover scheme in tandem with on-market offers. Such a combination has a number of advantages both to the offeror and to offeree shareholders, two of which are:

(a) offerees may elect between non-cash consideration under the takeover scheme (with however, the fuller escalation provisions of section 31 of the Code) and an immediate cash payment (after deduction of brokerage and stamp duty) under the on-market offers. Admittedly, the consideration under a takeover scheme might be paid in advance of the thirty day

---

38. Note 35 *supra*.

39. This is similar to the position of Peko-Wallsend Ltd in the offers by it pursuant to a takeover scheme for shares in Robe-River Ltd in 1983. Peko-Wallsend decided part way through the offer period to amend the offers so as to provide a two-tiered consideration, namely a base price per share if it did not become entitled to 90% or more of the issued shares in Robe-River and an enhanced price per share if it did become so entitled. In that case, as in the case under consideration, such a variation of offers required an order under s. 58 effectively excusing the offeror in this regard.

period specified in section 16(2)(f)(vii). Of course, where offers under the scheme remain subject to a "prescribed condition" which is not fulfilled or waived, such early payment may involve considerable risk to the offeror; and

(b) offerees who wish to ensure the identity of the purchaser of their shares may accept offers under the takeover scheme. This is in contrast to the position where offers are constituted by a takeover announcement and, as is increasingly the case, other persons enter the market at the same or a marginally higher price than the offer price.[40] These persons need not disclose their identify to the market (except possibly through an indirect disclosure by virtue of the substantial shareholder provisions and section 39 of the Code) while an offeree cannot prevent shares sold by him being allocated equally amongst all buyers at the same price (subject to the size of each of the broker's orders, the disclosure of which cannot generally be compelled under stock exchange rules).

Such combinations of offers pursuant to the mechanisms of the Code suggest a further combination which, to the knowledge of the writers, has not yet been adopted. This combination consists of a partial takeover run in conjunction with a full takeover (whether by way of a takeover scheme or an on-market announcement).

Various methods might be adopted for the framework of such dual offers. The first question is whether such a combination might be contained within the one set of offer documentation. There appears to be no obstacle to this in the "black letter" provisions of the Code and, in particular:

(a) sections 16(2)(a)(i) and 16(2)(a)(ii) are, strictly, cumulative rather than mutually exclusive alternatives, given the structure of section 16(2), and therefore full offers might be combined with partial offers under section 16(2)(a)(ii);
(b) assuming the full bid is also made by way of a takeover scheme, for the purpose of section 16(2)(f)(iii) the maximum number of shares proposed to be acquired is 100%; and
(c) it is possible that section 26 will not apply to assist the partial offers (if they are made under section 16(2)(a)(i)) because the offeror proposes to acquire all the shares in the target. Against this view, it is arguable that section 26 is simply a machinery provision which is intended to apply wherever a bid is made

40. For example the bid by FAI Insurance Ltd for shares in Alliance Holdings Ltd at $1.56 in competition with the on-market takeover by Mercantile Credits Ltd at $1.55.

under section 16(2)(a)(i) that is not a full bid. In this regard we note that section 26 operates so as to perfect section 16(2)(a)(i) partial bids, rather than by increasing the rights of the offeror (contrast section 42). Even if this argument is not correct, the problem can be cured either by proceeding by way of section 16(2)(a)(ii) for the partial offers or by seeking an order under section 58 amending the operation of section 26 appropriately. (It might also be possible to incorporate the provisions of section 26 in the terms of the offers themselves.)

As to section 60, none of the four criteria in section 60(1) and (3) are infringed by such a combination, since such a combination still requires the offeror to comply fully with the protective provisions of the Code.

Furthermore, it is strongly arguable that if dual partial and full offers are permitted under the Code shareholders are likely to be confused by two sets of offers by the same offeror running concurrently, but (we assume) at different levels of consideration and otherwise on different terms.

The next question concerns the drafting of such offers. For this purpose it will be assumed that the offer price under the partial offers exceeds that under the full offers.

One possibility (the "First Alternative") is to provide that the offerees cannot accept the partial offers without also accepting the full offers as to the balance of their shares.

A second possibility (the "Second Alternative") is to provide that offerees may accept the partial offers in the usual fashion and can choose to tick a box or otherwise signify a desire to accept the full offers as to the balance of their shares.

Alternatively, the offerees might be permitted to choose between the full offers and the partial offers, so that either they sell part of their shares at the (higher) partial offer price, or they sell all of their shares at the full offer price (the "Third Alternative").

Under the First Alternative, the offeror is, in effect, simply making full takeover offers at an average price per share in between the full and partial offer prices. However, such a combination may well be commercially more appealing than full offers at that average price.

The Second Alternative enables the offeror to exactly match competing partial offers while still providing a means of disposal of the balance of shares held by each offeree. If the partial offers can be accepted without having to accept the full offers, all other things being equal, the combined offers are in no way less

advantageous than the competing partial bid. In addition those offers enable each offeree shareholder to quit his holding in the target altogether.

The Third Alternative enables the offeror to match a competing partial offer, and to provide full takeover offers as an alternative, without involving it in the additional expense implied by the First Alternative. This type of combination of offers appears to be the most potent of weapons in the takeover arsenal.

The framework above assumes that both offers proceed by way of a takeover scheme whether or not in the same documentation. Alternatively, the partial offers might be dispatched pursuant to a takeover scheme while the full offers are constituted by an on-market announcement under section 17. There is nothing in the Code which appears to inhibit such a combination, subject to the comments below concerning section 40, and to the necessity of being careful to avoid activating the provisions in the Code concerning the 'flow-on' to accepting offerees of higher cash prices paid outside the takeover scheme or announcement.

In particular, there appears to be no ground on which the Commission might make a declaration under section 60(1) or section 60(3) (or, therefore, an order under section 60A(1)).

This is so for three reasons:

(a) both full and partial takeovers are authorised by the Code, and therefore in the absence of anything to the contrary, the combination of those takeovers is impliedly also authorised;

(b) the four criteria set out in section 60(1) and section 60(3) provide no basis for an adverse declaration. Indeed, an offeror making such combined offers may have to comply with all of the protective provisions of the Code twice over, unless both offers are contained in the same documentation; and

(c) it would appear that the interests of shareholders are best served by affording them an alternative between two offers, either of which could have been made independently and each of which will have some advantage to offerees; therefore the spirit of the Code would appear to encourage rather than to conflict with such a combination. Indeed, such a combination may well be regarded as ameliorating some of the harsher aspects of the partial takeover by providing a more palatable alternative for those shares not sold under the partial offers.

The advantages to offerors of such a combination are manifold and include the following:

(a) the partial takeover will (presumably) be made at a higher

price which is more likely to secure control of the company for the offeror, while at the same time the full offers enable offerees to quit their holding in the company altogether. At the least, offerees can choose between the partial offers and the full offers under the Second and Third Alternatives. However, under the First Alternative (and under the Second Alternative where offerees accept the full offers as to the balance of their shares) accepting offerees will probably receive an average price which is likely to contain some control premium. Contrast the position under partial offers alone, where the subsequent discount in value of shares not sold under the offers may erode some or all of any control premium contained in the offer price;

(b) a combination of offers in this fashion enables the offeror to rely on section 13(3) and to purchase shares in the ordinary course of trading on the stock exchange in the fourteen day period between the service of the Part A Statement and the commencement of the offer period;

(c) such a combination of offers also enables the offeror to rely on section 42 and to compulsorily acquire a dissenting minority. In this regard, note that section 42 merely requires that "before the end of the period during which the offers remain open, the number of shares ... to which the offeror is entitled became or becomes not less than 90% of the shares". Therefore, that entitlement need not be achieved exclusively by acceptances under either the full or the partial takeover; and

(d) perhaps the greatest advantage of such a combination is to enable an offeror wishing to make full offers to compete on equal or better than equal terms with a competing offeror making only partial offers. In the past the partial offeror has had a decided advantage in that it can probably afford to bid at a higher price per share than the full offeror. In this case shareholders might well be compelled to accept the partial offer and thereby ensure the defeat of the full offer by the failure of a minumum acceptance condition attached to the full offers. This remains the case even where an offeree would have been better off to have accepted the full offer as to all of his shares.

However, three difficulties attend upon such a combination of offers:

(a) It might be argued that the payment of a higher price under the partial offers or the earlier payment of consideration

under the full offers (where these are constituted by an on-market announcement) is in breach of section 40 of the Code. Since section 40(1) refers to "any benefit ... not provided for under the takeover offers" it appears that any benefit under one set of offers but not under the other set might be a benefit in breach of section 40. (Possibly this question does not arise where both full and partial offers are contained in the one Part A Statement and offer document.) Section 40(2) contains a parallel provision with respect to on-market announcements. There are three answers to this. The first is simply to argue that the purpose behind section 40 is to ensure that all shareholders are dealt with equally so that no special incentives to accept are given to particular offerees. In this case, the reference to "the takeover offers" (or "the takeover announcement") should be construed to include all offers or announcements made in accordance with the Code.

The second response to this difficulty (although one which we suggest is unnecessary in this regard) is to seek an order under section 58 of the Code from the NCSC varying the operation of section 40 so as to allow "benefits" provided under dual offers.

The third response is a partial solution only, in that it only relates to a breach of section 40 by virtue of the earlier payment of consideration under full on-market offers. In this case the exemption in section 40(3)(b) may be relied upon. Of course, any other prima facie breach of section 40 must still be cured in one of the ways mentioned above.

(b) Where the partial offers are of the type described as the Second Alternative, and are made under section 16(2)(a)(ii), the offeree who wishes to accept the partial offers *pro tanto* and the full offers for the balance of his shares will not know how many of his shares remain after his acceptance of the partial offers. This is a consequence of the operation of section 26 discussed above.

Two possible solutions to this problem are as follows:

(i) the partial offers could be framed under section 16(2)(a)(ii) so as to relate to a definite percentage of shares held by each offeree, leaving that offeree open to accept the full offers with respect to the remaining shares. This solution has the added attraction that some commercially useful purpose could finally be found for section 16(2)(a)(ii)!; and

(ii) the offers (and, in particular, the form of transfer and

acceptance) could be drafted so as to enable an offeree to accept the partial offers *pro tanto* and to accept the full offers with respect to an as yet indeterminable fraction, being the balance of his shares. This might be achieved by simply asking each offeree to tick a box indicating whether he wished to accept both of the offers in whatever proportion might eventuate.[41] Of course, this problem does not exist under the First or the (commercially superior) Third Alternative.

(c) The principal limitation governing such a combination of offers is to ensure that the higher price which is (presumably) payable under the partial offers does not feed through into the full offers. Three permutations exist under the price flow-on mechanisms set out in the Code.

(i) The easiest case to analyse is that where both the full and partial offers are made under a takeover scheme and where both offers are effected by the same documentation. All of the price flow-on mechanisms contained in the Code apply only where a higher consideration is paid other than under the offers. Therefore, if the same offers contain dual terms and alternative levels of consideration, it appears that no price flow-on difficulties exist since the wording of the relevant provisions gives those provisions no application where different levels of consideration are contained within the same offer document.

(ii) Where both the partial and full offers are made under takeover schemes, but those schemes are documented separately, the position is more complicated. The price flow-on mechanism concerning takeover schemes is contained in section 31 of the Code, and the various permutations which exist under this provision derive from the fact that the escalation provision contained in section 31 applies only in respect of a higher *all-cash* consideration paid outside the takeover scheme. Therefore, if either or both of the takeover schemes do not contain any

---

41. That this alternative is available is suggested by *Scott* v. *H.S. Lawrence & Son Pty Ltd* note 27 *supra*, in which it was said that an offeror was entitled to withdraw offers under s. 21 of the Code and simultaneously propose alternative contractual arrangements. Adapting that reasoning, offers drawn as proposed would at the same time leave a percentage of shares of each offeree outside acceptance of the partial offers, and propose terms upon which that balance of shares might still be acquired by the offeror.

all-cash alternatives, prices paid under either such scheme do not flow-on to offerees who accept under the other scheme. Assuming that the price payable under the partial offers is the greater, the flow-on mechanism of section 31 can be avoided by ensuring that the partial offer has some non-cash consideration attaching to each alternative available consideration. Where this is not commercially preferable in any case, it may still be achieved by offering a virtually all-cash consideration with a minor paper component.

(iii) Where both the full offers and the partial offers are all-cash, the purchase of any shares under either scheme will cause the consideration under that scheme to flow-on to offerees who accept under the other scheme, with the likely result that offerees may accept the full takeover offers as to all of their shares at the (higher) price payable under the partial offers.

Clearly therefore, it is necessary, in combining such offers, to ensure that the partial offer has a non-cash component whereas the full offer may be all-cash.

The position is similarly confused where the full offers are constituted by a takeover announcement. The relevant flow-on provision in that case is set out in section 17(6). This provision states that the price to be specified in a takeover announcement must be not less than the highest price per share "paid or agreed to be paid" for any share purchased or agreed to be purchased "in the 4 months immediately preceding the day of the announcement".

A number of limitations are contained in this provision:

(a) since offers constituted by a takeover announcement must provide for a cash-only consideration, it is doubtful that this provision has any operation where consideration under the partial takeovers has any non-cash element; and

(b) the triggering event is the purchase of, or entry into an agreement to purchase, any shares in the target by the offeror or any associate of the offeror. Therefore, the Part A Statement pursuant to which partial offers are to be made may be registered with the Commission between fourteen and twenty eight days in advance of the on-market announcement without any shares being purchased or agreed to be purchased under that partial takeover scheme, given that offers under the scheme need only be dispatched prior to the end of that period. If those offers are unconditional, acceptances of them

after such dispatch will create binding agreements to purchase those shares so as to trigger section 17(6), in which case the partial takeover offers must not be dispatched until after the day of the announcement.

If however those offers are conditional and contain, for example, a condition that none of the prescribed occurrences take place in relation to the target during the offer period, then no binding agreement to purchase shares will exist (assuming the condition is not waived) until the close of the offer period under the takeover scheme. In this case, the takeover announcement could be delayed until such time. Of course, where shares in the target are listed, the advantage of combined offers (namely that purchases can be made during the ordinary course of trading on a stock exchange even during the fourteen day period referred to in section 16(2)(d)) will be lost.

Once the takeover announcement has been made, increases in the price payable occur only by virtue of section 17(8) which, once again, would appear to have no operation where the subsequent price paid contains a non-cash element, and which in any case appears to be limited to prices paid on-market, as opposed to prices paid under offers dispatched pursuant to a takeover scheme.

It is less clear that section 17(9) has no application in relation to a price paid outside the takeover announcement where that price contains a non-cash element. Section 17(9) prohibits the payment during the last five days of the period of the takeover announcement of a price greater than that payable under the takeover announcement. However, even if this section applies where the higher price contains a non-cash element, or where offers under the partial takeover scheme provide an all-cash consideration, breach of this provision is avoided by simply extending the takeover announcement offer period[42] to ensure that no higher price is paid during the five day period referred to in section 17(9).

VI. CONCLUSION

The partial takeover is much maligned, and justifiably. The winner in a partial bid is invariably the bidder, while offeree

42. Where the partial offers remain subject to a prescribed condition so as to prevent a binding "agreement" arising from acceptance of them, an extension of the takeover scheme offer period may be made.

shareholders will be the losers. If indeed the Code is designed to protect offeree shareholders, partial bids should either be prohibited or regulated more effectively than they are at present.[43]

The writers consider that the only viable option open to the legislature is to prohibit partial takeovers except where specifically permitted by the NCSC, thus adopting protections of the type contained in the London Code. Until such amendments are made, partial takeovers will continue to be used with accelerating regularity to defeat full takeover offers and to wrest control of a company for deficient premiums.

43. It has recently been suggested that the inequities of the partial takeover could be removed by a "shark repellent" solution, involving a change of articles so as to remove voting rights of shares acquired pursuant to acceptances of a partial takeover, and pehaps even to provide for the compulsory divestiture of those shares at the instigation of the directors of the target. These restrictions might admit exceptions where a general meeting of shareholders approved the partial takeover by an ordinary resolution (somewhat reminiscent of the s. 12(g) resolution provided for under the Code) or where the holders of a majority of shares have signified their approval of the partial offers, much in the manner required under the London Code. G.J. Samuel and R.G. Grant, *Takeovers Mergers and Acquisitions 1984*, I.I.R. Conference 22-23 May, 1984. However this solution itself has a number of problems. The stock exchange to which the proposal was submitted was dissatisfied with it, which may preclude its adoption by listed companies. Probably the biggest drawback, however, is that such an arrangement will not be general to all companies and that the details of its execution from case to case will usually depend upon company directors, who are the likely initiators of such a proposal, and who have some incentive in drafting the new articles so as to be more restrictive than the interests of shareholders require.