



MEMO

To: Board of Directors
From: Company Secretary
Subject: **TAKEOVER APPROACH – CIRCUMVENTION**

You have advised that ABC (potentially, the 'bidder' for the Company's shares) has reached 'in principle' agreement with the Company's major shareholder (controlling 56%) on the terms/price to purchase their shares and so would like to acquire all other shareholdings on the same basis.

As I see it, the major challenge facing ABC is that because the Company has more than 50 shareholders (123 in fact) it must either launch a formal takeover bid or call a shareholders' meeting to approve the acquisition. The other major issue is that if they do not get 90% acceptances they would not be able to compulsorily acquire the balance and may be left with an 'unacceptable' (to them) percentage shareholding in the Company.

The question they are asking then, as I understand it, is can we (i.e., the Company and/or its directors) assist their acquisition efforts; in particular, are we able to 'arrange' for the number of shareholders to be reduced to 50 or less so as to circumvent the takeover provisions of the Corporations Act. A reduction by some 73 shareholders (60% of the total) may seem a very tall order.

As a matter of interest, the 73 smallest shareholders only hold 2.55% of the total shares which, incidentally, is less than the 3% creep provision under the takeover code allowed each 6 months. Also, it is noted that the top 20 shareholders have >90%, so the other 103 shareholders have <10%.

Frankly, I think this would be a very 'difficult' matter for us (i.e., the Company and/or its directors) to get involved in, for a number of reasons that jump to mind. By the way, none of my comments are supported by any legal references or specific knowledge and if ABC really wants us to 'assist' they should obtain and provide us with acceptable legal advices/clearance before we do anything.

Key Issues

The issues I see include:

1. Is it even appropriate for directors to be trying to assist a bidder's actions to acquire the Company's shares – directors represent all existing shareholders and are obliged to do the right thing by them.



2. In any case, it may well be incumbent on the directors to seek an independent valuation of the Company to assist shareholders in seeing the true worth/value of their shares and in coming to a decision on whether or not to accept the offered acquisition price for their shares.
3. If the idea is – before any formal approach from the bidder – for someone, or several persons, to acquire the ‘smaller’ shareholders so as to reduce the actual number of shareholders in the Company, then the question arises how might this be done. Also, if such actions were to occur then those acquirers may well be seen to be acting in concert – either together or with the bidder. Furthermore, if relevant, they may be restricted from acquiring more than 20% (the takeover ‘trigger’) themselves.
4. As touched on above, I really do not see how anyone could easily instigate a situation where one or several shareholders could approach other shareholders to buy their shares (or, vice versa, where some shareholders could approach others to sell their shares). This is probably the most critical hurdle in this proposal in that it is a fundamental tenet of the Corporations Act that generally shares in a company – other than where stock exchange listed – cannot be publicly offered (either as a new issue or later re-sale) without a prospectus (or other disclosure document). So, I believe the Company and/or its directors/officers may be prohibited under the Act from doing such a thing (i.e., ‘share hawking’ and/or promoting and/or assisting ‘secondary sales’). To my knowledge the only body/person who might possibly do that would be a licensed securities dealer/stock broker – and could/would they do it for an unlisted company in any case (this mechanism may only be available for listed companies).
5. I have heard there may be ways ‘around’ these provisions, such as seeking ASIC consent in certain circumstances. Also, if available (although most unlikely where 70+ shareholders may be involved to get the residual number down to no more than 50 shareholders), the exemption (from issuing a prospectus) provisions can also be applied towards secondary sales. Another way I believe potential bidders can ‘circumvent’ the Act is that some lawyers are prepared to draw up suitable documentation to allow the bidder to contract with the key shareholder(s) for them to be obliged to sell their shares on certain terms/conditions/price (eg, subject to shareholder approval, a minimum acceptance level, etc) should a takeover bid be launched – thereby giving the bidder some certainty that the transaction will in due course be completed to the bidders satisfaction.
6. The other key issue is what price might any such trades take place at? How can a ‘reasonable’ price be agreed? Could these trades be ‘undone’ if ABC does not end up completing its acquisition? And if the purchase price is paid over an extended period (eg, in 2 tranches, the latter portion being paid if/on meeting certain performance targets, etc) then how is that built into the equation?
7. Would all shareholders (both buyers and sellers) be aware before such action happens that there is a potential bid coming from ABC, and the terms of that. I think all shareholders must be made fully aware of the proposal as soon as possible, and certainly before anyone (either the bidder, or someone else) starts making an offer for their shares.



Summary

I trust the board finds my 'ramblings' of some use.

In summary, I see this whole idea – for the board/directors to aid a potential bidder in acquiring shares in the Company through what might be termed circumvention of the provisions of the Act – fraught with 'danger' and unknown issues, and I strongly recommend legal advice be sought before any decision is made to proceed to assist.

DISCLAIMER

The comments in this memo reflect some commercial aspects and observations on the matter experienced or observed by the writer in practice as he understands them. The information is given as a guide only and does not represent a definitive or legal view of any of the issues raised, covered or referred to and the reader is urged to seek his own professional advice on all aspects of, or pertaining to, this and any related matter.