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Dear Jennifer

### **Rule 16(b) Class Exemption**

1. The Society's Commercial and Business Law Committee (the Committee) welcomes the opportunity to comment on the consultation paper referred to above issued by the Takeovers Panel entitled "Rule 16(b) Class Exemption".
2. In this submission, the Committee comments principally on the draft exemption notice in Appendix B of the paper. Before commenting on the exemption notice, the Committee will comment on some issues of principle in paragraphs 3 to 5.

### **Matters of Principle**

3. The Committee favours option 2. If the Code is unduly restrictive, or inappropriate, in respect of transactions generally (as opposed to in respect of a specific transaction) then the correct approach is to amend the Code. The Committee appreciates the practical difficulties raised in paragraph 46 of the paper. Because of those difficulties, the practical solution is the class exemption notice proposed in option 3, on the basis that the Code will be amended at the first available opportunity, and that the class exemption will then be revoked.
4. The Committee does not support option 4. Paragraph 60 of the paper says, in respect of option 4:

*"This option proposes a class exemption as for option 3, but will also require an additional level of approval by the Panel. The Panel would approve that the proposed transaction fell within one of the exempted classes. The exemption could not be relied upon without first obtaining that Panel approval."*

Either a transaction will fall within "one of the exempted classes" specified in the exemption notice, or it will not. Like any other matter governed by the Code or by any other legislation or regulation, this is a matter of the proper interpretation of the words used in the legislation or regulation. If the Panel decides that the exemption notice has not been complied with in a particular case, it is open to the Panel to take enforcement action. Option 4 gives the Panel a discretionary power to decide that a

particular transaction, which would otherwise fall within the exemption notice, may not proceed in reliance on the exemption notice. That would:

- (a) lead to uncertainty in respect of the application of the Code for market participants and their advisers; and
- (b) result in cost for market participants in seeking the Panel's approval, and delay while the Panel is deciding whether or not to grant approval.

If any person has concerns as to whether or not they are able to comply with the exemption notice, it is open to them to raise that with the Panel.

5. For the same reasons, the Committee does not support provisions to the effect that the notice of meeting, or a statement in a company's annual report (which is discussed in more detail below), should be in a form approved by the Panel. The exemption notice can set out what the relevant statement is required to deal with. It is up to the company to comply with the notice. The extent to which the Panel is consulted, and approval sought, is a matter for individual market participants. Again, these provisions would in our submission lead to uncertainty, delay, and an undesirable degree of discretion for a regulatory authority.

#### **Appendix B -Draft Class Exemption Notice from Rule 16(b) of the Code**

6. Regarding the definition of “specified transaction”, paragraph (a) of this definition limits the transactions to which the exemption notice will apply to a rights issue, an underwriting arrangement, and the exercise of options. It is unclear why that should be the case. The position reached by the Panel is expressed in paragraph 27 of the paper:

*“... if the non-associated shareholders approve the potential maximum allotment of voting securities, then, by implication, the shareholders also approve any lesser percentage of voting rights that may be acquired as a result of the transaction.”*

If that concept is correct (and the Committee considers it is), then it applies whatever the nature of the transaction under which securities are to be issued. If the concern is that the exact number and percentage of voting securities to be issued should be expressed wherever it is possible to do so, that is already dealt with by paragraph (b) of the definition. Paragraph (a) of the definition should be deleted.

7. See the comments in paragraphs 4 and 5 above, with regard to clause 7(1)(c) and the reference to “approved by the Panel” in clause 8(2).
8. Clauses 8(2) and 8(3) provide for conditions which are within the control of the code company, rather than the allottee. If the code company fails to comply with them, the exemption notice will cease to apply, and voting securities cannot be allotted to the allottee without breach of the Code. For example:
  - (a) Company X issues to A options to subscribe for voting securities which, if exercised, will allow A to take control of company X.

- (b) The shareholders of company X pass a resolution under rule 7(d) approving the exercise of the options.
- (c) The board of company X later decides that it does not want A to acquire control of company X (possibly because it becomes clear that A will change the board).
- (d) The board of company X fails to comply with the conditions in clauses 8(2) and 8(3), and thereby effectively blocks A from exercising the options and taking control.

This is effectively a simple defensive tactic available to company X (although rule 38 would not apply because there is no takeover offer involved).

The Committee suggests that the Panel consider whether the exemption notice should be changed so that clauses 8(2) and 8(3) are a “term” (referred to in section 45(1) of the Takeovers Act), rather than a condition, and to make it clear that failure to comply with clauses 8(2) and 8(3) does not affect the application of the exemption notice.

- 9. With regard clause 9(2), clause 9 applies only if there is a change of control of the allottee that “results in an effective change of control of the allotting code company”. In general terms, this would be the case only if a party (together with its associates) held at least 50% of the voting securities of the allottee. However, approval is required to a change of control of a shareholder of a code company if that shareholder holds 20% or more of the voting securities. The Committee suggests that the Panel clarify what is meant by “an effective change of control”.
- 10. A question may arise where options are exercised in tranches and an event arises after say the exercise of one tranche but before the exercise of a second tranche where the exemption notice can no longer be relied upon. The Panel should make clear that the earlier allotments are valid.

### **The Panel's Questions**

- 11. Below are answers to the questions raised in paragraphs 77 to 84 of the paper.
- 12. *What classes of transaction should a class exemption from rule 16(b) cover?*

There is no reason to limit the exemption to any particular type of transaction. See paragraph 6 above.

- 13. *Should the class exemption be limited to a single allottee per exempted transaction?*

The exemption should not be limited so that it applies only to a single allottee per exempted transaction. The notice of meeting can adequately set out relevant details. If this approach were adopted, companies would need to structure transactions to have separate exempt transactions and call multiple meetings (each starting at the conclusion of the former meeting) to approve the allotment for each allottee. This would not be efficient.

14. *Should the class exemption be limited to transactions of short duration?*

There is no reason for so limiting the exemption. There is no time limit imposed by the Code between the passing of a resolution under rule 7(c) or 7(d) and the acquisition or allotment of securities authorised by that resolution. However, as noted in paragraph 10, the exemption specifies the consequences if circumstances change during the transaction.

If you have any queries regarding this submission, please contact Diana Brown, the Committee Secretary in the first instance, by phone 04 463 2967 or email [diana.brown@lawsociety.org.nz](mailto:diana.brown@lawsociety.org.nz).

Yours sincerely

A handwritten signature in black ink, appearing to read 'John Horner', written in a cursive style.

John Horner  
**Convener, Commerce and Business Law Committee**