

JOANNA BATE

**A COMPARISON OF THE LAW RELATING TO SCHEMES
OF ARRANGEMENT AND TAKEOVER OFFERS IN NEW
ZEALAND**

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Table of Contents

<i>I</i>	<i>Introduction</i>	4
<i>II</i>	<i>Rationale for Takeover Regulation</i>	8
<i>III</i>	<i>Code Takeovers</i>	9
	<i>A History of Takeover Regulation in New Zealand</i>	9
	<i>B The Takeovers Code</i>	10
	<i>C Code Takeovers</i>	11
	1 <i>Full takeover offers</i>	12
	2 <i>Compulsory acquisition</i>	13
<i>IV</i>	<i>Schemes of Arrangement</i>	14
	<i>A History of Schemes in New Zealand</i>	15
	<i>B The Current Scheme Regime</i>	17
<i>V</i>	<i>Analysis of Target Shareholder Protection</i>	22
	<i>A Fair Treatment of Shareholders</i>	22
	1 <i>Minority shareholder protection</i>	22
	2 <i>Consideration offered in the takeover</i>	25
	<i>B Ability to Decide on the Merits of a Takeover</i>	26
<i>VI</i>	<i>The Bidder's Choice of Mechanism</i>	27
	<i>A Certainty in the Outcome of the Takeover</i>	28
	1 <i>Minimum acceptance conditions</i>	28
	2 <i>Lock-up agreements</i>	29
	<i>B Acquiring 100 per cent Control</i>	30
	<i>C Flexibility</i>	32
	1 <i>Transaction structure</i>	32
	2 <i>Timeframe for the takeover</i>	32
	<i>D Bearing the Cost of the Takeover</i>	34
	<i>E An All or Nothing Mechanism</i>	35
	1 <i>Voting agreements and statements of voting intention</i>	36
	<i>F Only Applicable to Friendly Takeovers</i>	38
	1 <i>Due diligence</i>	38
	<i>G Splitting Shareholders into Interest Classes</i>	39
	<i>H Conclusion</i>	40

VII	<i>Potential for Reform</i>	40
<i>A</i>	<i>Who Must be Notified</i>	41
<i>B</i>	<i>Who is Entitled to Appear</i>	41
<i>C</i>	<i>Determination of Interest Classes</i>	41
<i>D</i>	<i>Information to be Provided to Shareholders</i>	42
<i>E</i>	<i>Shareholder Meetings</i>	43
<i>F</i>	<i>Timeframes</i>	43
<i>G</i>	<i>Shareholder Protection</i>	43
VIII	<i>Conclusion</i>	44

I Introduction

Owning shares in a company affords the holder of the shares certain rights against that company. While these rights “may be negated, altered, or added to by the constitution of the company”,¹ shares generally confer on the holder “the right to [one] vote on a poll at a meeting of the company on any resolution”.² The Companies Act 1993 (the CA) provides a non-exhaustive list of resolutions that a shareholder has the right to vote on. This list includes resolutions that appoint or remove a director, alter the company’s constitution or approve a major transaction.³ It follows that if a shareholder held a significant proportion of a company’s shares that shareholder would be able to wield control over the company through their ability to cast their votes on a resolution at a general meeting.⁴

It is often not necessary for a shareholder to hold a de jure majority (more than 50 per cent) of a company’s voting rights to be able to exercise this control.⁵ This is particularly so in “listed companies or companies with widely-held shareholdings” where “shareholders either find it difficult to exercise their voting rights or, as passive investors, are not sufficiently interested in the future direction of the company to exercise their votes”.⁶ In New Zealand, a shareholding that confers “more than 20 [per cent] of the voting rights” in a widely-held or listed company is deemed by legislation to be a significant enough shareholding to give a shareholder likely control over that company.⁷ Where more than 20 per cent of the voting rights (conferred by the holding or controlling of voting shares) in a company (the target) are acquired by another person (the bidder), control of the company changes hands.⁸ Change of control transactions like this are referred to as corporate takeovers.⁹

¹ Companies Act 1993, s 36(2).

² Section 36(1).

³ Section 36(1)(a).

⁴ Peter Watts, Neil Campbell and Christopher Hare *Company Law in New Zealand* (2nd ed, LexisNexis, Wellington, 2016) at 780.

⁵ Watts, Campbell and Hare, above n 4, at 780.

⁶ Watts, Campbell and Hare, above n 4, at 780.

⁷ Watts, Campbell and Hare, above n 4, at 780, n 10; and Takeovers Code Approval Order 2000, sch r 6(1)(a). Any subsequent references in this paper to the Takeovers Code are references to the rules and other provisions that are contained in the schedule of the Takeovers Code Approval Order 2000.

⁸ Takeovers Code, r 3(1) definition of “voting security”.

⁹ Takeovers Panel *Report of the Panel on the Takeovers Code* (June 1995) at 1.

In New Zealand, corporate takeovers are regulated primarily by the Takeovers Code (the Code) which contains the “rules applying to takeovers”¹⁰ of publicly listed or widely-held companies (known under the Code as code companies).¹¹ Fundamentally, the Code prohibits takeovers, as a result of a person acquiring more than 20 per cent of the voting rights in a code company, unless the takeover is done in accordance with the rules of the Code.¹² However, the law in New Zealand has developed in such a way that it is also possible for takeovers to occur under the CA using a scheme of arrangement (scheme). While schemes were for a time used to effect takeovers in a manner that avoided “triggering” the application of the Code rules,¹³ law reform in 2014 inserted additional provisions into the CA to prevent the use of schemes in this way and “better align the schemes procedure ... with the ... Code”.¹⁴ Therefore, in New Zealand, a takeover can occur either under the Code or as a scheme under the CA. This means that a bidder, when launching a takeover, must decide whether to proceed under the Code or under the CA. It is this choice that forms the basis of this paper.

Before proceeding it is important to note that under the Code there are a number of permitted ways in which a person may acquire “an increased percentage of the voting rights in a code company” above the 20 per cent threshold,¹⁵ however, this paper focusses on only one of these permitted methods, a full takeover offer, for two reasons.¹⁶ First, a full takeover offer is the most comparable transaction to a scheme because both are likely to involve the bidder seeking to acquire all of the shares (and the attached voting rights) in the target.¹⁷ This is in contrast to a partial takeover offer, where an offer is made for “less than all of the voting securities of a target”,¹⁸ and other acquisitions permitted under the Code where voting rights may be acquired from as few as one existing shareholder of the target.¹⁹ Second, because a takeover involves the change in control of a company, the rule of the

¹⁰ Takeovers Act 1993, s 19(1).

¹¹ Rule 3A.

¹² Rule 6.

¹³ Sacha Oudyn “Schemes of Arrangement under Part XV of the Companies Act 1993” (2006) 12 NZBLQ 50 at 63.

¹⁴ Takeovers Panel *Schemes of Arrangement Guidance Note* (17 August 2018) at [1.2].

¹⁵ Rule 7.

¹⁶ Rule 7(a). The terms “full takeover offer”, “takeover offer”, “full offer” and “offer” are used interchangeably throughout this paper but all refer to a full takeover offer under r 7(a) of the Takeovers Code.

¹⁷ See Takeovers Code, r 8; *Re Fliway Group Ltd* [2017] NZHC 3216; *Re Nuplex Industries* [2016] NZHC 1677; and *Re Trilogy International Ltd* [2018] NZHC 580.

¹⁸ Rule 9(1).

¹⁹ Rule 7(c).

Code that relates to a person acquiring further voting rights, where they already hold more than 50 per cent, is of little relevance to the discussion because control of the company is already in that shareholder's hands.²⁰

It is also important to note that there are two key differences between a takeover offer and a scheme. The first is that an offer is in essence a “contract between the bidder and the target shareholders”²¹ under which the target shareholders have individually decided to accept the bidder's offer to acquire their shares.²² In contrast, under a scheme it is the target company board who present the arrangement to the target shareholders which proposes the acquisition of their shares by the bidder.²³ Therefore, under an offer the target board have little involvement in the takeover,²⁴ whereas, under a scheme it is the bidder who has less involvement once the scheme is proposed.²⁵ Takeovers effected by schemes are often referred to as “friendly” takeovers because they rely on the target board cooperating with the bidder to prepare the arrangement before it is proposed to target shareholders.²⁶ This is in comparison to a takeover offer which does not require any collaboration between the bidder and the target board during the takeover process. The lack of any necessary collaboration can cause a takeover under the Code to occur in a hostile, rather than friendly, manner.²⁷ The second key difference is that, the process for a takeover offer is prescribed solely by the rules of the Code,²⁸ whereas, the process for a scheme is governed by both the CA and the court.²⁹ Under a scheme, two court hearings are required, the first for direction on any procedural matters and the second for the court to make a decision whether to sanction the scheme.³⁰ In between the two hearings the target shareholders must also vote in interest classes on whether to approve the scheme.³¹

²⁰ Rule 7(e).

²¹ Jennifer Payne *Schemes of Arrangement: Theory, Structure and Operation* (Cambridge University Press, Cambridge (UK), 2014) at 89.

²² See Takeovers Code, r 8; and Payne, above n 21, at 91.

²³ Payne, above n 21, at 86.

²⁴ Payne, above n 21, at 89.

²⁵ See Payne, above n 21, at 104.

²⁶ See Jennifer Payne “Schemes of Arrangement, Takeovers and Minority Shareholder Protection” (2011) 11 JCLS 67 at 70.

²⁷ Payne, above n 21, at 102.

²⁸ Takeovers Act, s 22(b).

²⁹ Companies Act 1993, ss 236-237.

³⁰ Takeovers Panel *A Basic Guide for Shareholders about the Takeovers Code* (October 2018) at 5.

³¹ Takeovers Panel, above n 30.

Schemes are fast becoming the “most popular way to conduct friendly takeovers” in New Zealand.³² Since the Code was implemented in 2001, schemes were used for around 7 per cent of all takeovers but in more recent years this percentage has grown.³³ In the years following the 2014 reform of the CA scheme provisions, schemes were used for 23 per cent of all takeovers and in 2017, the year prior to writing, schemes were used in 50 per cent of all takeovers.³⁴ This paper explores this developing trend by comparing schemes with takeover offers.

Following the introduction in Part I, Part II of this paper provides background on the rationale for the regulation of takeovers. This background focusses on understanding why New Zealand has a shareholder-centric approach to takeover regulation under which “the protection of shareholder interests” is paramount.³⁵ Parts III and IV of this paper explain the law relating to takeover offers and schemes respectively, including the process for effecting a takeover under both mechanisms. Part V of this paper considers whether, given the increased use of schemes to effect takeovers, shareholders are adequately protected when a takeover occurs by way of a scheme in comparison to the Code’s paradigm of shareholder protection. This paper submits that, particularly as a result of the 2014 reform of the CA, shareholders are sufficiently protected under the scheme process. Given that shareholders are adequately protected under both mechanisms, Part VI of this paper then discusses some of the advantages and disadvantages of a scheme when compared to a takeover offer to understand why a bidder may choose to structure a takeover as a scheme rather than an offer. This paper concludes this comparison by submitting that while there are arguable advantages and disadvantages to both mechanisms, on balance, both are capable of producing a similar outcome for the bidder. Through the analysis and discussion in this paper, there is one aspect of the scheme process that stands out as a potential area for further reform, namely, the need for two court hearings for a scheme to be approved. Part VII of this paper submits that the need for two court hearings has become unnecessary given the rising popularity of schemes. As this paper discusses at various points, the scheme process requires the court to exercise their discretion when considering a scheme however, following the 2014 reform of the CA and an emerging clear precedent set by the court in recent scheme cases, it is arguable that much of this discretion no longer necessary. This

³² MinterEllisonRuddWatts “Schemes of Arrangement” (21 February 2018) <<https://minterellison.co.nz>>.

³³ Bell Gully *Takeovers Market Practice Report* (June 2017) at 2.

³⁴ Bell Gully, above n 33, at 6; and Bell Gully *The Big Picture: Takeovers update* (March 2018) at 2.

³⁵ Julia Mignone “Is there sufficient protection for shareholders in a members’ scheme of arrangement? An analysis of the Eggleston principles and s 411(17) of the Corporations Act 2001 (Cth)” (2016) 30 *Aust Jnl of Corp Law* 259 at 260.

paper submits that the CA should be reformed so that any procedural matters, currently addressed in the first court hearing, form part of the legislation removing the need for the two-step court process making the scheme process more efficient.

II Rationale for Takeover Regulation

Takeovers as a result of the “acquisition of a controlling interest in a target company by another person”³⁶ “can give rise to significant unfairness” for shareholders for two reasons.³⁷ First, because the bidder can acquire “de facto control over a company ... with significantly fewer shares”³⁸ than a de jure majority the bidder.³⁹

... can use their *de facto* control to effect or block changes that impact upon all the shareholders without first having expended the necessary effort or capital to acquire *de jure* control of the company.

Second, because in takeovers “bidders [are] willing to pay extraordinarily high premiums”⁴⁰ above the market value of the target’s shares to acquire control, if the bidder only paid the premium price to a certain proportion of the target shareholders, in order to acquire de facto control, a number of shareholders would not be able to “participate in the control transaction” nor “receive their proportionate part of the value of control”.⁴¹

It is for these reasons that takeovers are regulated to ensure “that all shareholders get the opportunity to share in the payment of a control premium”⁴² and “dispose of their shares”⁴³ rather than remaining in the company following a change in control finding the value of their shares reduced on the basis that they now only hold “a minority stake”.⁴⁴

³⁶ Scott Clune “Amalgamations, Schemes of Arrangement and Takeovers Regulation: Concerns of the Takeovers Panel and the Need for Reform” (2007) 13 *Canta LR* 91 at 92.

³⁷ Watts, Campbell and Hare, above n 4, at 780.

³⁸ David Kershaw *Principles of Takeover Regulation* (Oxford University Press, Oxford, 2016) at ch 8.04.

³⁹ Watts, Campbell and Hare, above n 4, at 780.

⁴⁰ John C Coffee “Regulating the Market for Corporate Control: A Critical Assessment of the Tender Offer’s Role in Corporate Governance” (1984) 84 *Colum L Rev* 1145 at 1162.

⁴¹ Kershaw, above n 38, at ch 8.34.

⁴² John Armour and David A Skeel “Who Writes the Rules for Hostile Takeovers, and Why? - The Peculiar Divergence of U.S. and U.K. Takeover Regulation” (2007) 95 *Geo LJ* 1727 at 1737 (footnotes omitted).

⁴³ Kershaw, above n 38, at ch 8.28 (footnotes omitted).

⁴⁴ Andrew Johnston “Takeover Regulation: Historical and Theoretical Perspectives on the City Code” 66(2) *CLJ* 422 at 446.

As a result, New Zealand has a shareholder-centric approach to the regulation of takeovers.⁴⁵ This means the protection of “shareholder interests should be the first priority” of takeover regulation.⁴⁶ In New Zealand this protection is enshrined in the objectives of the Code, specifically that the Code assist in “ensuring that the holders of financial products in a takeover are treated fairly” and recognise that the “holders of financial products must ultimately decide for themselves the merits of a takeover offer”.⁴⁷ The meaning of financial product, “in relation to a code company”, encompasses not only shares that confer a voting right, but all shares in a company.⁴⁸ Therefore, the Code protects all shareholders, not just those who the bidder is acquiring control from.

In addition to protecting shareholders, the regulation of takeovers also strives to achieve a number of other objectives which include, “encouraging the efficient allocation of resources”, “encouraging competition for the control” of companies, “promoting the international competitiveness of New Zealand’s capital markets” and “maintaining a proper relation between the costs of compliance [with regulation] and the benefits resulting from it”.⁴⁹

III Code Takeovers

A History of Takeover Regulation in New Zealand

Takeovers have been regulated in New Zealand since the enactment of the Companies Amendment Act 1963. This amendment Act inserted into the Companies Act 1955 (the predecessor to the current CA) the procedure for a bidder company to follow “when making a ‘take-over offer’” to a target company.⁵⁰ However, this regulation had its limitations. For example, it “only applied to offers made in writing and did not apply to acquisitions made through the stock exchange”.⁵¹ Additionally, there was no “specific supervisory body” created to oversee compliance with the regulation so “compliance was labelled ‘optional’”.⁵² The legislation was also criticised for how it treated minority shareholders

⁴⁵ Mignone, above n 35, at 261.

⁴⁶ Mignone, above n 35, at 260.

⁴⁷ Takeovers Act, ss 20(1)(c) and 20(1)(e).

⁴⁸ Takeovers Act, s 2 definition of “financial product”.

⁴⁹ Takeovers Act, s 20(1).

⁵⁰ Clune, above n 36, at 92.

⁵¹ Clune, above n 36, at 92 (footnotes omitted).

⁵² Clune, above n 36, at 92 (footnotes omitted).

“in the context of a change of control”⁵³ and for failing to adequately encourage “competition for control of companies”.⁵⁴

To remedy the shortcomings, New Zealand company law went through substantial reform in 1993 with the enactment of the Takeovers Act 1993 (the TA), the CA and the Companies Act Repeal Act 1993 (that repealed the earlier Companies Amendment Act 1963). Included in the TA, was the creation of a regulatory body, the Takeovers Panel (the Panel).⁵⁵ One of the Panel’s early tasks was to “formulate and recommend a takeovers code”⁵⁶ to the government which led to the creation of the Code that came into force, albeit a number of years later, in 2001.⁵⁷ The Panel have a number of functions including responsibility for enforcing compliance with the Code.⁵⁸

B The Takeovers Code

The Code provides a set of rules for takeovers that seek “to promote ... workable and effective takeover activity and, at the same time, provide an increased measure of participation and equal treatment for shareholders”.⁵⁹ The Code applies to all companies that fall within the meaning of a code company and cannot be contracted out of.⁶⁰ A code company is a company that:⁶¹

- (a) is a listed issuer that has financial products that confer voting rights quoted on a licensed market; or
- (b) was within paragraph (a) at any time during the period of 12 months before a date or the occurrence of an event referred to in this code; or
- (c) has 50 or more shareholders and 50 or more share parcels.

The fundamental rule of the Code prohibits a person from acquiring more than 20 per cent of the voting rights in a code company or, holding or controlling an increased percentage of the voting rights where that person already “holds or controls 20 [per cent] or more of the voting rights” unless they comply with the Code.⁶² It is important to note that the

⁵³ Clune, above n 36, at 93.

⁵⁴ Clune, above n 36, at 92.

⁵⁵ Takeovers Act, s 5.

⁵⁶ Takeovers Panel, above n 9, at 4.

⁵⁷ Takeovers Code, r 1.

⁵⁸ Takeovers Panel *A Basic Guide for Directors about the Takeovers Code* (October 2018) at 13; and Takeovers Act, s 8.

⁵⁹ Takeovers Panel, above n 9, at 5.

⁶⁰ Rule 5.

⁶¹ Rule 3A(1).

⁶² Rule 6(1).

fundamental rule not only applies to a person who holds voting rights but also to a person who controls voting rights. Control, “in relation to a voting right, means having, directly or indirectly, effective control of the voting right.”⁶³ Additionally, in calculating whether a person holds or controls 20 per cent of the voting rights in a company, the fundamental rule also takes into account any voting rights that an associate of that person may hold or control.⁶⁴ Therefore, if a person along with an associate, holds or controls more than 20 per cent of the voting rights in a code company they will be in breach of the fundamental rule.⁶⁵

The prohibition on holding or controlling more than 20 per cent of the voting rights in a code company extends beyond just the acquisition of shares to include:⁶⁶

... situation[s] where control increases by any means. In some cases, such as a cancellation of securities, a reorganisation of voting rights attaching to shares, or, a share buy-back transaction, an increase in control triggering the Code could occur involuntarily on the part of the controller. Hence, the Code is outcome focussed and, ... defines ‘takeover’ as a change in control effected by any means whatsoever.

C Code Takeovers

The fundamental rule has a number of exceptions to allow takeovers to occur.⁶⁷ These exceptions allow a person to acquire more than 20 per cent of the voting rights in a code company so long as the acquisition is done in a manner that is compliant with the rules of the Code.

The Code provides that a person can acquire more than 20 per cent of the voting rights in a code company by making a full or partial offer, by an acquisition or allotment approved by an ordinary resolution of the code company,⁶⁸ “under a creeping acquisition”⁶⁹ (where a person already holds or controls more than 50 per cent but less than 90 per cent of the voting rights) by acquiring no more than a further 5 per cent of the voting rights in each 12-month period,⁷⁰ or “by means of a compulsory acquisition if the shareholder holds 90

⁶³ Takeovers Code, r 3 definition of “control”.

⁶⁴ Rule 6.

⁶⁵ See rule 4 meaning of “associate”.

⁶⁶ Clune, above n 36, at 101.

⁶⁷ Rule 7.

⁶⁸ Rule 7(a)-(d).

⁶⁹ Clune, above n 36, at 95.

⁷⁰ Rule 7(e).

percent or more of the code company”.⁷¹ As noted in Part I, this paper focusses on full offers, therefore in the proceeding discussion only full takeover offers are discussed.

1 Full takeover offers

To acquire more than 20 per cent of the voting rights in a code company a bidder can make a full offer. The offer must be for all of the target’s shares “whether voting or non-voting”⁷² and “must be conditional on the [bidder] achieving control of more than 50 percent of the voting rights in the company”.⁷³ The procedure for making an offer is as follows.

First, the bidder must send written notice to the target that they intend to make a takeover offer along with the terms and conditions of that offer.⁷⁴ An offer “may be subject to any conditions, except those that depend on the judgement of the [bidder]”.⁷⁵ The terms of the offer must “specify the period for which [the offer] will remain open”⁷⁶ which must “be not shorter than 30 days, and not longer than 90 days”.⁷⁷ The offer period is subject to these constraints to ensure that shareholders have “adequate time to make their decision” whether to accept the offer.⁷⁸ An offer period may only be extended in limited circumstances as provided for in the Code.⁷⁹ An offer “must be made on the same terms and provide the same consideration for all [shares] belonging to the same class of [shares] under offer”.⁸⁰ Where there is more than one class of shares included in the offer, the bidder must also provide to the target an independent adviser’s report with the takeover notice.⁸¹ This report must include advice on whether “the consideration and terms offered for each class” of shares is “fair and reasonable between the classes” and in relation to non-voting shares, “is fair and reasonable in comparison with the consideration and terms offered” for the voting shares.⁸² Within a period of 14 to 30 days after the takeover notice the bidder must then send the offer to the target shareholders.⁸³

⁷¹ Clune, above n 36, at 95 (footnotes omitted); and Takeovers Code, r 7(f).

⁷² Rule 8.

⁷³ Clune, above n 36, at 95.

⁷⁴ Rule 41; and Takeovers Code, sch 1 cl 5.

⁷⁵ Rule 25.

⁷⁶ Rule 24.

⁷⁷ Rule 24(2)(b).

⁷⁸ Takeovers Panel, above n 58, at 6.

⁷⁹ Rules 24A-24C.

⁸⁰ Rule 20.

⁸¹ Rule 22.

⁸² Rule 8(3)-(4); and Takeovers Code, sch 3.

⁸³ Rules 43 and 43B.

Second, the target must provide to the bidder and the target shareholders a target company statement.⁸⁴ The target company statement must include, amongst other things, “a recommendation by the directors of the target company” as to whether shareholders should accept or reject the offer or “a statement that the directors ... are unable to make, or are not making a recommendation” and their reasoning for the recommendation.⁸⁵ In addition, the target must also provide to shareholders a copy of an independent adviser’s report “on the merits of an offer”.⁸⁶ A copy of the takeover notice, offer, target company statement and any independent adviser’s reports must also be sent to the Panel at the same time as they are sent to the relevant parties as specified above.⁸⁷

At the end of the offer period, if the offer has received a sufficient number of acceptances from the target shareholders and any conditions of the offer are met, the takeover is successful.

2 *Compulsory acquisition*

Where, as a result of a takeover offer, the bidder “becomes the holder or controller, ... of 90 [per cent] or more of the voting rights in [a] code company”, the bidder becomes, what is known as, the dominant owner of the target.⁸⁸ As the dominant owner, the bidder “has the right to acquire all the outstanding [shares] in the code company” under the compulsory acquisition rules of the Code.⁸⁹

Once the bidder has crossed the 90 per cent threshold the bidder must send written notice to the remaining target shareholders to notify them that they are now the dominant owner.⁹⁰ As the dominant owner the bidder has, either, the right to compel “the outstanding [shareholders] [to] sell their [shares] in the code company” to the bidder or, the bidder must advise “the outstanding [shareholders] [that they] have the right to sell their [shares] in the code company to the dominant owner”.⁹¹ In the case of becoming the dominant owner as the result of an offer, where the bidder acquires the remaining shares in the target, the

⁸⁴ Rule 46.

⁸⁵ Takeovers Code, sch 2 cl 15(1).

⁸⁶ Rule 21; and Takeovers Code, sch 2 cl 19.

⁸⁷ Rule 47.

⁸⁸ Rule 50, definition of “dominant owner”.

⁸⁹ Rule 52.

⁹⁰ Rule 51.

⁹¹ Rule 55(1)(b).

“consideration payable in respect of [shares] in any class must be the same as the consideration provided under the offer”.⁹²

The compulsory acquisition rules enable the bidder to acquire 100 per cent control of the target, if they wish, by compelling any remaining minority shareholders, who did not initially accept the offer, to sell their shares. However, the rules are also protective because they enable the remaining minority shareholders to sell their shares in return for the same consideration that was payable under the offer and are therefore not disadvantaged because they did not initially accept the offer. Additionally, the rules give the remaining minority shareholders a “right of exit”,⁹³ so they are not left “stuck in the target company”⁹⁴ where they may risk being subject to oppressive or other adverse conduct at the hands of the bidder who now has control of the target.⁹⁵

IV Schemes of Arrangement

As introduced in Part I of this paper, takeovers can also occur under the CA using a scheme. In fact, before the “adoption of the Takeovers Code” schemes were recognised as “an appropriate method of carrying out a takeover”.⁹⁶

There are two key differences between a takeover effected by a scheme and a takeover offer, as noted in Part I of this paper. The first is that a scheme is an arrangement “proposed between a company” and its shareholders whereas,⁹⁷ a takeover offer is in essence a “contract between the bidder and the target shareholders”.⁹⁸ A takeover effected by a scheme involves the target company board presenting an arrangement to the target shareholders which generally proposes the acquisition of all of the target company’s shares by a bidder in return for some specified consideration.⁹⁹ The second is that the scheme process is reliant on the court, rather than just on a process prescribed by legislation.¹⁰⁰

⁹² Rule 56(1).

⁹³ Payne, above n 26, at 82.

⁹⁴ Payne, above n 26, at 78.

⁹⁵ Payne, above n 26, at 83.

⁹⁶ Clune, above n 36, at 101.

⁹⁷ Payne, above n 21, at 83.

⁹⁸ Payne, above n 21, at 89.

⁹⁹ See for example, *Re Fliway Group Ltd* above n 17; *Re Nuplex Industries*, above n 17; and *Re Trilogy International Ltd*, above n 17.

¹⁰⁰ See Companies Act 1993, ss 236-237.

A *History of Schemes in New Zealand*

Historically, under English law, schemes were court approved arrangements “between a company in liquidation and its creditors”,¹⁰¹ before being extended to include solvent companies and then further extended to include arrangements between a company and its shareholders.¹⁰² Schemes in New Zealand have “largely followed the English precedent”.¹⁰³

The New Zealand legislation relating to schemes is found in the various iterations of the Companies Act.¹⁰⁴ Prior to the current regime, the procedure for schemes was contained in the Companies Act 1955.¹⁰⁵ This Act defined “arrangement” as meaning:¹⁰⁶

... a [reorganisation] of the share capital of the company by the consolidation of shares of different classes or by the division of shares into shares of different classes, or by both those methods.

Case law has widened the meaning of “arrangement” to include any arrangement that could “reasonably be regarded as commercially desirable in the interests of the company as a whole”.¹⁰⁷ This broad interpretation of “arrangement” led to the use of schemes becoming a mechanism to effect takeovers.¹⁰⁸

Under the 1955 Companies Act, where a scheme was proposed between a company and its shareholders, on application to the court, the court would order a meeting of shareholders (or any interest class of them) to consider the arrangement.¹⁰⁹ At the time of being summoned to the meeting, shareholders were also sent a statement “explaining the effect of the ... arrangement”.¹¹⁰ If, at the court ordered meeting, 75 per cent of the shareholders

¹⁰¹ Oudyn, above n 13, at 51.

¹⁰² Oudyn, above n 13, at 52.

¹⁰³ Oudyn, above n 13, at 52.

¹⁰⁴ See Companies Act 1933, ss 159-161; Companies Act 1955, ss 205-207; and Companies Act 1993, ss 235-239.

¹⁰⁵ Companies Act 1955, ss 205-207.

¹⁰⁶ Section 205(5).

¹⁰⁷ *Re Milne & Choyce Ltd* [1953] NZLR 724 (SC); and *Re Milne & Choyce Ltd* [1953] NZLR 724 (CA) at 746.

¹⁰⁸ Oudyn, above n 13, at 53.

¹⁰⁹ Companies Act 1955, s205(1).

¹¹⁰ Section 206(1)(a).

affected by the scheme voted to approve it, the scheme was then considered by the court.¹¹¹ As part of the court's consideration of the scheme:¹¹²

... the Court was required to take into account a number of matters including whether the scheme was such that an intelligent person of business might reasonably approve and whether the scheme was fair and reasonable to all affected parties.

The arrangement, if sanctioned by the court, then became binding on all shareholders and the company.¹¹³

In 1993, company law in New Zealand went through considerable reform which resulted in the enactment of the current CA. As part of this reform, the scheme procedure that was contained in the 1955 Companies Act was split into two approaches.¹¹⁴ The first approach, now found in pt 13 of the CA, deals with the amalgamation of companies and employs “a prescriptive approach whereby a 75 [per cent] vote at a meeting of shareholders could bring about an amalgamation without court sanction”.¹¹⁵ The second approach, now found in pt 15 of the CA, provides for a “court-sanctioned scheme of arrangement”.¹¹⁶ The pt 15 scheme procedure was intended to be used as “a broad backup ... where the prescriptive approach” of pt 13 “was not practical”.¹¹⁷ However, in reality, the two approaches formed alternative and “completely different mechanisms that [could] perform similar tasks”.¹¹⁸ The scheme provisions gave the court “vast discretion” to determine, “with no guidance from the legislation”, “the extent to which meetings” of shareholders were required, the voting “majorities required” to approve a scheme and “the information required to be disclosed” to shareholders.¹¹⁹ The “intelligent business person and fair and equitable test” for approval of a scheme continued to apply.¹²⁰

As a result of the 1993 reforms, a takeover of a code company in New Zealand could occur under the Code, under pt 13 of the CA as an amalgamation or under pt 15 of the CA as a

¹¹¹ Section 205(2).

¹¹² Clune, above n 36, at 99 (footnotes omitted).

¹¹³ Section 205(2).

¹¹⁴ Clune, above n 36, at 99.

¹¹⁵ Clune, above n 36, at 99.

¹¹⁶ Clune, above n 36, at 100.

¹¹⁷ Clune, above n 36, at 99.

¹¹⁸ Clune, above n 36, at 100.

¹¹⁹ Clune, above n 36, at 100.

¹²⁰ *Weatherston v Waltus Property Investments Limited* [2001] 2 NZLR 103 (CA) at [35].

scheme. The broad court discretion and lack of guidance contained in the pt 15 provisions led to schemes becoming a way to “avoid triggering” the rules of the Code,¹²¹ that normally applied to takeovers, and in doing so undermined the objectives of the Code.¹²² The most notable example of this was the merger between code companies Independent Newspapers Limited (INL) and Sky Network Television Limited (Sky). INL and Sky entered into a scheme where:¹²³

... a new company (Newco) acquired all the shares in INL and Sky in return for ... consideration issued to the shareholders of INL and Sky. In order to avoid the jurisdiction of the ... Code the scheme provided for the cancellation of all Sky and INL voting rights immediately before the shares were acquired by the Newco. Accordingly, no person became the holder or controller of voting rights in [a] ... code company as a result of the scheme, even though Newco acquired all the shares in the two code companies.

B The Current Scheme Regime

In response to the use of schemes as a method to avoid the Code, company law went through further legislative reform. The Companies Amendment Act 2014 inserted additional provisions into pts 13 and 15 of the CA relating to code companies.¹²⁴ First, an additional section was inserted that prohibits a code company from amalgamating, under pt 13, unless it is a short form amalgamation (which involves a merger between a wholly owned subsidiary and its parent company).¹²⁵ Second, two new sections were added into pt 15 in relation to schemes that affect the voting rights of a code company.¹²⁶ Importantly, a scheme that affects the voting rights of a code company now cannot be approved by the court unless either “the court is satisfied that the shareholders of the code company will not be adversely affected by the use” of a scheme rather than the Code or the Panel must have indicated to the court that they have no objection to the court approving the scheme in a no-objection statement.¹²⁷ Additionally, rather than leaving it to the court’s discretion, where a scheme affects the voting rights of a code company, the CA now specifies the voting majorities required to approve a scheme at the shareholder vote including that a 75

¹²¹ Oudyn, above n 13, at 63.

¹²² Adam Bennett “Companies disguise takeovers to dodge rules” (4 April 2006) NZ Herald <www.nzherald.co.nz>.

¹²³ Takeovers Panel *Schemes of Arrangement and Amalgamations Involving Code Companies Recommendations to the Minister of Commerce* (August 2006) at [47].

¹²⁴ Section 219; and ss 236A-236B.

¹²⁵ Section 219(2); and s 222.

¹²⁶ Sections 236A-236B.

¹²⁷ Section 236A(2)(b).

per cent majority must be achieved in each interest class of shareholders.¹²⁸ It is also important to note that the new CA provisions apply to any situation where voting rights in a code company are affected (and therefore cover situations like the INL and Sky merger where voting rights were cancelled), as opposed to just situations where a person increases their holding of voting rights.¹²⁹ The procedure for a scheme that affects the voting rights of a code company is as follows.

First, an originating application is made to the court for the approval of the scheme and the Panel must be notified of the application.¹³⁰ The requirement for the Panel to be notified means that the Panel is able to “assist the court” in their consideration of the scheme by “reviewing scheme documents” and “helping to ensure that matters ... relevant to the Court’s decision are brought to the Court’s attention”.¹³¹

Along with applying to the court for the approval of a scheme, a target company is also able to apply to the Panel for a no-objection statement.¹³² The purpose of a no-objection statement is to confirm that the Panel do not object to the scheme proceeding.¹³³ Before providing a no-objection statement the Panel must be satisfied that “all material information ... has been disclosed” to shareholders, “the standard of disclosure ... has been equivalent to the standard required by the Code”, “interest classes of shareholders were adequately identified” and “there are no other reasons for the Panel to object to the scheme”.¹³⁴ The Panel will only provide a no-objection statement for schemes “that are accompanied by an independent adviser’s report” which covers “the merits of the proposed transaction” and addresses any issues of fairness between interest classes of shareholders under the scheme.¹³⁵ No-objection statements are usually issued just before the final court hearing so as an interim step, prior to the first court hearing (the first hearing is discussed below), the Panel, if they are satisfied with the information they have been provided in relation to the scheme, provide a letter of intention which confirms that they have “formed an initial view” on the scheme and intend “to issue a no-objection statement”.¹³⁶ Where the target company does not apply for a no-objection statement, “or if the Panel does not intend

¹²⁸ Section 236A(4).

¹²⁹ Section 236A(1).

¹³⁰ Section 236; s 236A(1); and High Court Rules 2016, 19.2(c).

¹³¹ Takeovers Panel, above n 14, at [1.7].

¹³² Takeovers Panel, above n 14, at [1.8].

¹³³ Takeovers Panel, above n 14, at 20.

¹³⁴ Takeovers Panel, above n 14, at [3.4].

¹³⁵ Takeovers Panel, above n 14, at [2.7]; and see Takeovers Code, r 22.

¹³⁶ Takeovers Panel, above n 14 at 19.

to issue a no-objection statement” the Panel may “seek to be heard at the initial Court” hearing.¹³⁷ In the absence of a no-objection statement, the Panel at the first hearing, “may object to the scheme or [may] ask the Court to make orders on ... the information to be provided to shareholders or the identification of interest classes”.¹³⁸

As the CA still gives the court some discretion on what is required for a scheme, an interlocutory application is included as secondary claim with the originating application. The interlocutory application enables the court to provide direction on any procedural steps, by way of initial orders in a first court hearing, that need to be completed before the court can consider approving the scheme.¹³⁹ Included in the initial orders are directions that cover who must be notified of the scheme, who is “entitled to appear and be heard on the application”, the make-up of shareholder interest classes, the information to be provided to shareholders and when the information must be provided.¹⁴⁰ The court also makes an order that meetings of shareholders, in interest classes, be held for the purposes of considering and voting on the scheme and when these meetings must be held.¹⁴¹

After the first hearing, at the court ordered meetings, the target shareholders consider the scheme and vote on whether to approve it.¹⁴² Before 2014, the voting majorities required to approve a scheme were at the court’s discretion, however following the 2014 reform, the shareholder approval thresholds required for a scheme (in relation to a code company) are now specified in the CA. The CA provides that a scheme must be approved “by a majority of 75 [per cent] of the votes of the shareholders in each interest class entitled to vote and voting on the question” and “by a resolution approved by a simple majority of the votes of those shareholders entitled to vote”.¹⁴³

Following the shareholder meeting and vote, a second court hearing is held. At the second hearing, a four-part test is employed by the court to assess the scheme.¹⁴⁴ This test requires the court be satisfied, before making the decision to approve a scheme, that:¹⁴⁵

¹³⁷ Takeovers Panel, above n 14 at [2.4].

¹³⁸ Takeovers Panel, above n 14 at [2.4].

¹³⁹ See for example, Fliway Group Limited *Notice of Meeting and Scheme Booklet* (21 November 2017) at 99.

¹⁴⁰ See Companies Act 1993, s 236(2).

¹⁴¹ Section 236(2)(b).

¹⁴² Section 236A(2)(a).

¹⁴³ Section 236A(4).

¹⁴⁴ *Re CM Banks Ltd* [1944] NZLR 248 (SC) at 248. See also *Re Milne & Choyce Ltd*, above n 107.

¹⁴⁵ *Re Nuplex Industries*, above n 17, at [10].

- (a) there has been compliance with the statutory provisions as to meetings, resolutions, the application to the Court, and the like;
- (b) the scheme has been fairly put to the class or classes concerned, and that if a circular or circulars have been sent out, as is usual, whether before or after the making of the application to the Court, they give all the information reasonably necessary to enable the recipients to judge and vote upon the proposals;
- (c) the class was fairly represented by those who attended the meeting and that the statutory majority are acting bona fide and are not coercing the minority in order to promote interests adverse to those of the class whom they purport to represent; and
- (d) the arrangement was such that an intelligent and honest person of business, a member of the class concerned, and acting in respect of his or her interest, might reasonably approve it.

In consideration of the “fourth limb of the ... test the court must also consider whether the proposed arrangement is generally fair and equitable”.¹⁴⁶

The first limb of the test ensures that there has been compliance with the statutory procedure contained in the CA and with the court’s initial orders. The court considers how “interested parties (and in particular shareholders) were informed of the scheme, and whether they had the opportunity to oppose it”, whether the shareholder meetings were “conducted in accordance with” the court’s direction,¹⁴⁷ and whether the arrangement was approved by the requisite shareholder majorities in correctly identified interest classes.¹⁴⁸

The second and third limbs ensure that shareholders were fully informed and fairly represented at the court ordered shareholder meeting. Under these limbs, the court considers whether the information provided to shareholders “fairly and fully” explains the scheme, “its intended effect ... and the reasons why” the target directors either recommended that shareholders vote in favour or against the scheme.¹⁴⁹ The court also considers whether shareholders were fairly represented at the shareholder meeting by looking at factors such as shareholder turnout to vote on the scheme, the support the scheme received, the absence of any shareholder notices of opposition and any other evidence to suggest the votes cast “were anything other than bona fide”.¹⁵⁰

¹⁴⁶ *Re Nuplex Industries*, above n 17, at [11] (footnotes omitted).

¹⁴⁷ *Re Nuplex Industries*, above n 17, at [14]-[15].

¹⁴⁸ *Re Nuplex Industries*, above n 17, at [17].

¹⁴⁹ *Re Nuplex Industries*, above n 17, at [20].

¹⁵⁰ *Re Nuplex Industries*, above n 17, at [22].

The court, under the fourth limb of the test, must then consider whether “the scheme [is] one that an intelligent and honest person of business, ... might reasonably approve” along with being “generally fair and equitable”.¹⁵¹ To make a conclusion on the fourth limb, the court takes into account factors such as the amount of shareholder support for the scheme, the views of the target directors, the lack of any prejudice to the target creditors or shareholders and the independent adviser’s report (if a report has been obtained).¹⁵²

Overlaying the four-part test above is the additional CA requirement that the court must be “satisfied that the shareholders of the code company will not be adversely affected by the use” of a scheme “rather than the takeovers code”¹⁵³ or there must have been a statement “filed from the ... Panel indicating that the ... Panel has no objection” to the scheme.¹⁵⁴ In practice, although it is not a mandatory requirement to obtain a no-objection statement, it is very likely that a no-objection statement will be obtained. In fact, at the time of writing, in all but one of the scheme cases that involved a code company, a no-objection statement was obtained from the Panel.¹⁵⁵ In the one case that did not, the court relied on the conclusion of the analysis under the four-part test to also conclude that the use of a scheme had “not adversely affected the interests of ... shareholders”.¹⁵⁶ It is important to note that even if the Panel provides a no-objection statement, the court does not have to approve the scheme “merely because the Panel has no objection” to it, the court have the ultimate discretion whether to sanction a scheme.¹⁵⁷

Finally, if all the statutory requirements are met and the elements of the four-part test are satisfied, the court can make an order approving the scheme. Once the court makes an order to approve a scheme “that affects the voting rights of a code company” the rules of the Code no longer apply to the transactions involved in implementing the scheme.¹⁵⁸ It is important to note that the Code continues to apply until the court makes its final orders, so

¹⁵¹ *Re Nuplex Industries*, above n 17, at [23].

¹⁵² *Re Nuplex Industries*, above n 17, at [24]- [28].

¹⁵³ Section 236A(2)(b)(i).

¹⁵⁴ Section 236A(2)(b)(ii).

¹⁵⁵ *Re Fliway Group Ltd*, above n 17, at [18]; *Re Trilogy International Ltd*, above n 17, at [8]; *Re New Zealand Oil & Gas Ltd* [2017] NZHC 809 at [6]; *Re Radius Properties Ltd* [2017] NZHC 473 at [12]; *Re Trustpower Ltd (No 2)* [2016] NZHC 2499 at [10]; *Re Nuplex Industries*, above n 17, at [9]; *Re Michael Hill International Ltd* [2016] NZHC 1393 at [7]; and *Re Scott Technology Ltd* HC Auckland CIV-2015-404-2332, 6 April 2016 at [6].

¹⁵⁶ *Re New Zealand Oil & Gas Ltd* [2015] NZHC 39 at [22].

¹⁵⁷ Section 236A(3).

¹⁵⁸ Section 236B.

parties to a scheme must be careful not to breach any rules of the Code when organising a scheme.¹⁵⁹

V Analysis of Target Shareholder Protection

The interests of target shareholders, subject to a takeover offer, are protected by the objectives of the Code, specifically that the Code must ensure “that the holders of financial products in a takeover are treated fairly” and that the “holders of financial products must ultimately decide for themselves the merits of a takeover offer”.¹⁶⁰ Part V of this paper analyses how the law relating to schemes measures up against the protections afforded to shareholders under the Code. This analysis focusses on two themes based on the objectives of the Code. First, whether shareholders receive fair treatment under a scheme in comparison to under the Code (including an analysis of minority shareholder protection and the consideration offered in a scheme). Second, whether the information provided, to enable shareholders to decide on the merits of a takeover, under a scheme equals the information provided under the Code.

A Fair Treatment of Shareholders

1 Minority shareholder protection

It is arguable that a scheme provides minority shareholders with less protection than a takeover offer. This is primarily because of the voting thresholds required for a scheme to be approved. As discussed in Part IV of this paper, a scheme, that will generally result in the bidder acquiring all of the shares in the target, must be approved by “a majority of 75 [per cent] of the votes of the shareholders in each interest class entitled to vote and voting” on the scheme and “by a resolution approved by a simple majority of the votes of those shareholders entitled to vote”.¹⁶¹ Whereas, a takeover offer that results in the bidder being able to acquire 100 per cent control requires acceptances to the offer by a sufficient number of shareholders to confer at least 90 per cent of the target’s voting rights on the bidder.¹⁶² This difference in shareholder support arguably creates minority shareholder oppression because “the minority [are] ... bound” by a scheme which has been approved by a lesser percentage of the target’s shareholders than is required under a takeover offer.¹⁶³ However,

¹⁵⁹ Takeovers Panel, above n 14, at [4.12].

¹⁶⁰ Takeovers Act 1993, s 20(1).

¹⁶¹ Companies Act 1993, s 236A(4).

¹⁶² Takeovers Code, r 50 definition of “dominant owner”.

¹⁶³ Payne, above n 26, at 72.

to overcome this, the scheme process provides a number of additional safeguards that protect minority shareholders.

First, minority shareholders are protected by the requirement that shareholders consider and vote on the scheme in interest classes. The shareholders who make up an interest class must have rights that are “sufficiently similar” enough to allow them to sensibly “consult ... about a common interest”.¹⁶⁴ This common interest, in relation to a scheme, is based on the “similarity and dissimilarity of shareholders’ legal rights against the company” under the proposed scheme.¹⁶⁵ Therefore, where a scheme proposes to “treat ... groups of [shareholders] ... differently, then it may well be that they need”¹⁶⁶ to be split into different interest classes for the purposes of considering and “voting on the scheme”.¹⁶⁷ An example of differential treatment is discussed below in relation to consideration under a scheme. Voting in separate interest classes means that any shareholders who are arguably being treated unfairly, as a result of differential treatment under a scheme, will have greater voting power in a separate interest class than they would if they voted in a class with shareholders who are not subject to this unfairness (and are perhaps more likely to approve the scheme). This is because, for a scheme to be approved it requires 75 per cent approval in each interest class. Therefore, a scheme may be able to be defeated by an interest class of shareholders if the vote in that interest class failed to reach 75 per cent approval.

Shareholders also have the protection of the court and the Panel where the question of determining interest classes is concerned. This is because “one of the key issues for the court” in the first hearing is to direct the target on “whether [shareholders] ... should be split” into different interest classes.¹⁶⁸ Additionally, regardless of whether a no-objection statement has been applied for, the Panel, either in a no-objection statement or at the first court hearing will provide their view on the determination of interest classes.¹⁶⁹ Therefore, shareholders have the assurance that they are voting on the scheme in a class of shareholders with similar interests under the scheme, as determined by legislation, the court and the Panel.

¹⁶⁴ Companies Act 1993, sch 10.

¹⁶⁵ Schedule 10.

¹⁶⁶ Payne, above n 26, at 91.

¹⁶⁷ Takeovers Panel, above n 14, at [2.15].

¹⁶⁸ Payne, above n 26, at 88.

¹⁶⁹ Takeovers Panel, above n 14, at [2.4]; and see Takeovers Panel, above n 14, at 20.

Second, included in the court's initial orders is a direction as to "the persons who shall be entitled to appear and be heard" on the scheme application.¹⁷⁰ Generally, those who can appear and object to the scheme include any target shareholders, the target company, the Panel, the bidder and "any other person who considers they have a proper interest in the Scheme and who wishes to appear and be heard on the Application for Final Orders".¹⁷¹ Therefore, if there are any concerns around minority oppression or unfairness under the scheme, shareholders of the target or any other "interested ... parties ... have the right to attend the final ... hearing" and if they wish, "present submissions and evidence to the court in opposition of the scheme" which the court will factor in to their final decision.¹⁷²

Third, directors "when exercising powers or performing duties, must act in good faith and in what the director believes to be the best interests of the company",¹⁷³ in addition to exercising "the care, diligence, and skill that a reasonable director would exercise in the same circumstances".¹⁷⁴ Therefore, the duties imposed on the directors of a company act as an additional "mechanism for shareholder protection" because the board must ensure they are acting in accordance with their duties when they propose a scheme to target shareholders.¹⁷⁵

Finally, the minority arguably have the greatest protection in the final court hearing where the court assesses the scheme and decides whether or not to sanction it. The final court hearing is "intended to serve as a safeguard against minority oppression of shareholders" because it requires the court to "carefully consider and scrutinise all ... circumstances".¹⁷⁶ Key to this consideration is that the court must be satisfied that the scheme is "at least so far fair and reasonable, as that an intelligent and honest man, ... in respect of his interest ... might approve it".¹⁷⁷ Other examples of the circumstances the court may consider were discussed in Part IV of this paper in relation to the four-part test that is employed by the court before deciding to approve a scheme. Therefore, the court's discretion and ability to "refuse to sanction a scheme if minority oppression is present" at the final hearing is "a significant protection for shareholders".¹⁷⁸

¹⁷⁰ Section 236(2)(e).

¹⁷¹ *Re Nuplex Industries* HC Auckland CIV-2016-404-1191, 10 June 2016 at [25]-[27].

¹⁷² Mignone, above n 35, at 277.

¹⁷³ Companies Act 1993, s 131.

¹⁷⁴ Companies Act 1993, s 137.

¹⁷⁵ Mignone, above n 35, at 278.

¹⁷⁶ Mignone, above n 35, at 272.

¹⁷⁷ *Re Alabama, New Orleans, Texas and Pacific Junction Railway Company* [1891] 1 Ch 213 (CA) at 247.

¹⁷⁸ Mignone, above n 35, at 276; and Payne, above n 26, at 88.

Therefore, even though there is a difference in shareholder support required for a scheme, compared to under a takeover offer, there are additional protections for minority shareholders under the scheme process to compensate for this. This paper submits that these additional protections put schemes on a level footing with the protections afforded to minority shareholders under the Code.

2 *Consideration offered in the takeover*

When a takeover offer is made, “the offer must be made on the same terms and provide the same consideration for all [shares] belonging to the same class of [shares] under offer”.¹⁷⁹ In addition, “the consideration ... offered for each class of ... [shares]” under the offer must be “fair and reasonable between the classes”¹⁸⁰ of shares and in relation to non-voting shares, “is fair and reasonable in comparison with the consideration and terms offered for voting [shares]”.¹⁸¹ The assessment of whether the consideration is fair and reasonable is done in an independent adviser’s report which is provided to the target along with the takeover notice.¹⁸² However, because schemes, once approved are not subject to the rules of the Code, it is possible for “differential consideration to be offered to shareholders” under a scheme.¹⁸³

The ability for a scheme to offer differential consideration causes a divergence between the law relating to schemes and the rules of the Code. Despite this, the Panel, in their consideration of a scheme (and decision whether to provide a no-objection statement) may not object to differential treatment so long as the issue of differential consideration is “covered in [an] independent adviser’s report”,¹⁸⁴ the “terms of the scheme ... ensure that the interests of ... shareholders are appropriately protected” and “the disclosure of the differential consideration” is adequate.¹⁸⁵ Requiring the view of an independent adviser on the issue of consideration brings schemes into line with the Code which also requires an independent adviser’s report.

To ensure the interests of shareholders are appropriately protected, where differential consideration is offered under a scheme, shareholders will generally be required to vote on

¹⁷⁹ Takeovers Code, r 20.

¹⁸⁰ Rule 8(3).

¹⁸¹ Rule 8(4).

¹⁸² Rule 22.

¹⁸³ Takeovers Panel, above n 14, at [2.20].

¹⁸⁴ Takeovers Panel, above n 14, at [2.22].

¹⁸⁵ Takeovers Panel, above n 14, at [2.20].

the scheme in interest classes that may be determined based on the consideration they are to receive under the scheme.¹⁸⁶ By requiring shareholders who are to receive less consideration under a scheme to vote in a separate interest class, their interests are protected because they must vote to approve the scheme by a 75 per cent majority in that interest class for the scheme to succeed. Therefore, if unfairness existed in the differential consideration offered under the scheme, an interest class of shareholders who were subject to this unfairness could prevent the scheme from proceeding by voting against it. However, the Panel have indicated that in some situations, that the Panel are able to provide guidance on, “it may be possible for shareholders to vote in the same interest class despite having differential entitlements under a scheme if the shareholders can sensibly consult with each other” about the scheme.¹⁸⁷

Therefore, although the rules of the Code and the law relating to schemes diverge on the issue of differential consideration, shareholders are still adequately protected under a scheme because of the need to for shareholders to vote on and approve the scheme in correctly composed interest classes and by the requirement that all material information is disclosed to shareholders to allow them to “ultimately decide for themselves the merits” of the scheme.¹⁸⁸

B Ability to Decide on the Merits of a Takeover

Prior to the changes to the legislation relating to schemes in 2014, the information that was required to be disclosed to shareholders in their consideration of a proposed scheme was “left to the Court to decide with no guidance from the legislation”.¹⁸⁹ The amendments that were made to the CA in 2014 have had the effect of aligning the disclosure requirements for schemes more closely with the requirements for a takeover offer under the Code through the Panel’s increased involvement in the scheme process.¹⁹⁰

Under a takeover offer, as discussed in Part III of this paper, the bidder must send to the target shareholders an offer document that contains the terms and conditions of the offer along with an independent adviser’s report where there is more than one class of shares included in the offer.¹⁹¹ In response the target company are required to provide to the bidder

¹⁸⁶ See Takeovers Panel, above n 14, at [2.21].

¹⁸⁷ Takeovers Panel, above n 14, at [2.21].

¹⁸⁸ Takeovers Act, s 20(1)(e).

¹⁸⁹ Clune, above n 36, at 100.

¹⁹⁰ Takeovers Panel, above n 14, at [1.2].

¹⁹¹ Rules 22 and 43.

and target shareholders a target company statement which includes an independent adviser's report on the merits of the takeover offer.¹⁹² The Code stipulates exactly what information must be provided in these documents to ensure the target shareholders are fully informed before making a decision as to whether to accept the bidder's offer.¹⁹³

Whereas, for a scheme it is the court who provide direction to the target company as to what information must to be provided to shareholders. The court direction is necessary to ensure that shareholders have "adequate information to make an informed decision" because the CA is silent on exactly what information must be provided to shareholders.¹⁹⁴ Additionally, since the 2014 changes to the CA, the target company, when applying for a no-objection from the Panel statement, are now able to work with the Panel to "agree the disclosures that should be made in the scheme documents".¹⁹⁵ Involved in this exercise is a "clause-by-clause analysis of the extent to which disclosures required" by the Code can be made in the scheme documentation, including an analysis of the information that is required in a takeover notice, takeover offer document and target company statement.¹⁹⁶ If a no-objection statement has not applied for, the Panel are still able to apply to be heard at the first court hearing and provide their view on what information should be disclosed to shareholders.¹⁹⁷

Given that the court provide direction as to what information must be provided to shareholders in the first hearing and the Panel (either by way of a no-objection statement or by appearing at the first court hearing) use the Code as reference to review and form an opinion on the proposed scheme documentation, it is submitted that shareholders are no better or worse off in terms of the information they receive in relation to a takeover regardless of the mechanism by which the takeover proceeds.

VI The Bidder's Choice of Mechanism

The ability to structure a takeover as an offer or a scheme raises the question, why would a bidder choose one over the other? Part VI of this paper explores this choice by discussing some of the advantages and disadvantages of both mechanisms.

¹⁹² Rules 21 and 46; and Takeovers Code, sch 2 cls 19.

¹⁹³ See, Takeovers Code, schs 1 and 2.

¹⁹⁴ Mignone, above n 35, at 271.

¹⁹⁵ Takeovers Panel, above n 14, at [2.5].

¹⁹⁶ Takeovers Panel, above n 14, at [2.6]; and see Takeovers Code, sch 1.

¹⁹⁷ Takeovers Panel, above n 14, at [2.4].

A Certainty in the Outcome of the Takeover

A scheme arguably provides the bidder with greater certainty over the outcome of a takeover. This is because once a scheme is approved it becomes binding “on the company and on such other persons ... as the court may specify”.¹⁹⁸ Where a scheme is used for a full takeover of the target, by way of acquiring all of the target’s shares, once approved, the scheme is binding on the target, the bidder and all of the target shareholders.¹⁹⁹ This gives the bidder certainty that they will acquire all of the shares in the target.

In contrast, the outcome of a takeover offer is less certain. Where the bidder makes an offer, the offer must be conditional on “receiving acceptances ... that, when taken together with voting [shares] already held or controlled by” the bidder, confers on the bidder “more than 50 [per cent] of the voting rights in the target”.²⁰⁰ Therefore the success of an offer is dependent on a sufficient number of target shareholders accepting the offer. An offer can result in three outcomes for the bidder. First, if the bidder crosses the 50 per cent threshold and is successful in obtaining acceptances from at least 90 per cent of the target shareholders, the bidder will be able to compulsorily acquire any remaining shares in the target and gain 100 per cent control.²⁰¹ Second, if the bidder crosses the 50 per cent threshold but does not reach 90 per cent, the takeover will succeed, but the bidder will not be able to acquire 100 per cent control. In this situation, if the bidder was seeking 100 per cent control, the outcome of the takeover may not be as successful as the bidder may have initially hoped, but they will still acquire control and a de jure majority stake in the target. Or third, if at the end of the offer period, the bidder has failed to cross the 50 per cent threshold, because an insufficient number of shareholders have accepted the offer, the takeover will fail. Therefore, under an offer, the outcome of the takeover will be uncertain until the offer period ends.

1 Minimum acceptance conditions

To mitigate this uncertainty, the bidder can choose to make an offer “conditional on a level of acceptances” so long as this level is more than the 50 per cent threshold.²⁰² For example, the bidder may make an offer conditional on receiving acceptances that confers on the bidder more than 90 per cent of the voting rights in the target. A minimum acceptance condition of this kind allows the bidder to utilise the compulsory acquisition rules and

¹⁹⁸ Companies Act 1993, s 236(1).

¹⁹⁹ See *Re Trilogy International Ltd*, above n 17, at [47].

²⁰⁰ Takeovers Code, r 23.

²⁰¹ Rule, 55(1).

²⁰² Payne, above n 21, at 94.

subsequently acquire the remaining 10 per cent of the voting rights in the target and gain 100 per cent control.²⁰³ If a minimum acceptance condition is set above 50 per cent, the offer may also include a right for the bidder to waive this condition and make the offer conditional simply on receiving 50 per cent control.²⁰⁴ While this may improve the likelihood of a successful takeover, it may also mean the bidder does not acquire the percentage of control that they set out to gain and instead has to settle for somewhere less than 100 per cent control.

2 *Lock-up agreements*

In addition to minimum acceptance conditions, the uncertainty surrounding the outcome of a takeover offer can be further mitigated through the use of lock-up agreements. Lock-up agreements are “legal commitment[s] by shareholder[s] ... to accept a takeover offer” that are “generally entered into prior to the public announcement of a takeover offer”.²⁰⁵ Lock-up agreements give the bidder certainty that the offer will be accepted by the locked-up shareholders which can go a long way to ensuring the success of a takeover.²⁰⁶ In fact, since the Code came into force, lock-up agreements have been used in just over half of all takeover offers with an average locked-up stake of 45 per cent.²⁰⁷ Importantly, all full takeover offers that included lock-up agreements were successful.²⁰⁸

The success of a takeover offer can be almost guaranteed if a lock-up agreement is used in conjunction with a pre-offer stake, held by the bidder, in the target. For example, if a bidder held a 20 per cent pre-offer stake (the most possible without breaching the fundamental rule of the Code) and locked-up a further 45 per cent, (the average locked-up stake) the 50 per cent minimum threshold will have been met without needing any further shareholder acceptances, therefore, so long as any other conditions to the offer were satisfied, the takeover will succeed.

Lock-up agreements are permitted by the Code but are subject to constraints.²⁰⁹ First, lock-up agreements must clearly state that the bidder is excluded from becoming the controller of the voting rights attached to the locked-up shares, until the offer is declared

²⁰³ See Takeovers Code, pt 7.

²⁰⁴ See rr 24B and 24C.

²⁰⁵ Takeovers Panel *Guidance Note on Lock-up Agreements* (3 May 2016) at [1].

²⁰⁶ Takeovers Panel, above n 205, at [2].

²⁰⁷ Bell Gully, above n 33, at 17.

²⁰⁸ Bell Gully, above n 33, at 17.

²⁰⁹ Takeovers Panel, above n 205, at [2].

unconditional, so not to breach the fundamental rule.²¹⁰ Second, locked-up shareholders “cannot obtain terms or consideration” under the offer that differ from the terms or consideration “offered to other shareholders” in the offer.²¹¹ This means that there is no unfair advantage given to the locked-up shareholders in return for their commitment to accept the takeover offer over non-locked-up shareholders.

Therefore, while schemes arguably provide the bidder with greater certainty over the outcome of a takeover, the outcome of a takeover offer can be made more certain through the use of minimum acceptance conditions and lock-up agreements.

B Acquiring 100 per cent Control

Schemes arguably make it easier for the bidder to gain 100 per cent control over the target company. As mentioned above, this is because a scheme that proposes a full takeover of the target, if approved by the target shareholders and the court, will result in the bidder obtaining 100 per cent control of the target.

For a scheme to be approved by the target shareholders, the proposed scheme must be approved by a 75 per cent majority “of the votes of the shareholders in each interest class entitled to vote and voting on the question” and by a “simple majority of the votes of those shareholders entitled to vote”.²¹² This results in the bidder being able to acquire 100 per cent of the shares in the target with less than 100 per cent shareholder approval. It is important to note that the 75 per cent majority required to approve the scheme relates to a 75 per cent majority of those shareholders who actually voted on the proposed scheme, therefore, in reality a scheme may be approved by far less than 75 per cent of the target shareholders if a number of shareholders do not vote on the scheme. In theory, a scheme, that would bind all shareholders, could be approved by target shareholders whose votes made up as little as 51 per cent of all of the target’s voting rights so long as they cast all their votes in approval of the scheme. However, as mentioned in Part IV of this paper, if voter “turnout ... is very low this might be a factor for the court to take into account when determining whether [or not] to sanction the scheme” at the final hearing.²¹³

In contrast, under an offer, the bidder must first have become the dominant owner of the target, by way of being the holder or controller “of 90 [per cent] or more of the voting

²¹⁰ Takeovers Panel, above n 205, at [4].

²¹¹ Takeovers Panel, above n 205, at [5].

²¹² Companies Act, s 236A(4).

²¹³ Payne, above n 21, at 96, n 75.

rights in the” target “by reason of acceptances of [the] offer”²¹⁴ before being able to acquire the remaining 10 per cent of the voting rights and gain 100 per cent control.²¹⁵ Even if, prior to making the offer, the bidder held a pre-offer stake in the target (20 per cent at the most), the bidder would still need to acquire at least a further 70 per cent (87.5 per cent of the remaining voting rights outside of those held by the bidder) of the voting rights to cross the 90 per cent threshold.

The disparity in target shareholder support required to acquire 100 per cent control between a scheme and an offer arguably causes schemes to be the more attractive option where the bidder wants to acquire 100 per cent control. However, this advantage arguably has a reciprocal disadvantage in that the voting thresholds may make it is easier for minority shareholders to block a takeover from proceeding under a scheme than under an offer. Shareholders who hold a 25 per cent stake in the target will “have the power to vote down [a] scheme” but in reality, a blocking stake may be much lower than this.²¹⁶ This is because, the 75 per cent threshold required is based on shareholders who actually vote on the scheme, therefore if voter turnout is low, a shareholding less than 25 per cent will be sufficient to stop a scheme.²¹⁷ In comparison, under an offer, if the bidder did not hold a pre-offer stake, at least 50 per cent of the target shareholders would have to reject the offer to block the takeover and stop the bidder from receiving sufficient acceptances to cross the 50 per cent minimum threshold.²¹⁸ Even if the bidder held a pre-offer stake of 20 per cent, at least 30 per cent of the target shareholders would need to reject the offer to stop the bidder from crossing the 50 per cent threshold.

Therefore, although a scheme may make it easier for the bidder to acquire 100 per cent control, it is also easier for minority or dissentient shareholders to defeat a scheme than an offer. If the bidder “is willing to go ahead with less than 100 per cent control ... and there is a concern about dissentient shareholders, it may be better to use an offer”.²¹⁹ However, as discussed above, minimum acceptance conditions and lock-up agreements may increase the likelihood of an offer achieving sufficient shareholder support to reach the 90 per cent threshold and subsequently utilise the compulsory acquisition rules to gain 100 per cent control.

²¹⁴ Takeovers Code, r 50 definition of “dominant owner”.

²¹⁵ Rule 52.

²¹⁶ Payne, above n 21, at 102.

²¹⁷ Payne, above n 21, at 101.

²¹⁸ Payne, above n 21, at 101.

²¹⁹ Payne, above n 21, at 102.

C Flexibility

1 Transaction structure

Schemes arguably provide greater flexibility in the structure of the takeover transaction than is permissible under the Code because the Code only provides for a limited number of exceptions to the fundamental rule.²²⁰ These exceptions have the effect of limiting the types of transactions that are capable under the Code.

Takeovers effected by a scheme will often involve the bidder acquiring all of the shares (and attached voting rights) in the target, in a similar way that shares are acquired under an offer, but this is not always the case.²²¹ The broad definition of “arrangement”, as discussed in Part IV of this paper, means that a scheme may involve transactions other than, or in addition to, an acquisition of shares. For example, a takeover effected by a scheme may occur as a result of a “compulsory buyback” by the target “of all ordinary shares held” by all shareholders other than the bidder (where the bidder holds a pre-scheme stake). A scheme of this kind has the effect of increasing the voting rights held by the bidder from their pre-scheme stake to 100 per cent.²²² In addition, schemes may be used to effect a re-domiciliation of a code company,²²³ a return of capital,²²⁴ or a demerger, all of which may also involve a change in control of the target company.²²⁵ While it is arguable that the flexibility in the transaction structure is an advantage of effecting a takeover as a scheme, both schemes and offers can be used to effect a change in control, therefore, both mechanisms are capable of producing the desired result for the bidder, the takeover transaction itself may just take a different form.

2 Timeframe for the takeover

Although there are a number of requirements that must be met before a scheme can be approved there are no defined timeframes within the CA for when these requirements must be met.²²⁶ In contrast, the requirements for an offer are subject to a number of restrictive timeframes. For example, once the bidder has given the target notice of its intention to

²²⁰ Rule 7.

²²¹ See *Re Fliway Group Ltd*, above n 17; *Re Nuplex Industries*, above n 17; and *Re Trilogy International Ltd*, above n 17.

²²² *Re Radius Properties Ltd*, above n 155; and Takeovers Panel “Radius Properties Limited” <takeovers.govt.nz>.

²²³ See *Re Michael Hill International Ltd*, above n 155.

²²⁴ See *Re New Zealand Oil & Gas Ltd*, above n 156.

²²⁵ See *Re Trustpower Ltd (No 2)*, above n 155.

²²⁶ Takeovers Panel, above n 30, at 5.

make an offer, the offer must be sent to the target shareholders between 14 and 30 days after the notice,²²⁷ and then once the offer is made it must remain open for at least 30 days but cannot be open for longer than 90 days, except in limited circumstances.²²⁸

The flexibility in the timeframe for a scheme is arguably an advantage for the bidder. This is particularly so in situations where consent for the takeover to proceed may be required from other regulatory bodies such as the Commerce Commission or the Overseas Investment Office (OIO).

This flexibility was necessary in the recent takeover, by way of a scheme, of Scott Technology Limited (Scott) by JBS Australia Pty Limited (JBS). In this case, consent was required from the OIO before the scheme could be approved because JBS were investing in Scott who had the ownership of a piece of land, that fell within the meaning of sensitive land under the Overseas Investment Act 2005, in addition to the investment being in significant business assets.²²⁹ By the time the OIO granted consent,²³⁰ it had been 152 days since the scheme documentation was provided to shareholders (which is analogous to the date an offer is made to shareholders under an offer).²³¹ It was 159 days after the scheme was put to shareholders that the scheme received final court approval (which is analogous to when an offer becomes unconditional).²³² If JBS had used an offer, rather a scheme, the maximum number of days JBS would have had from making the offer to declaring it unconditional is 120 days, that is, a maximum of 90 days for the offer to remain open plus a maximum of 30 days after the offer period to declare the offer unconditional (because the takeover required OIO approval).²³³ Therefore, if JBS had used an offer instead of a scheme, it is likely that the offer would have lapsed, due to the length of time it took to receive OIO approval, causing the takeover to fail.

While the flexibility in the timeframe for a scheme is arguably an advantage, an offer may still be the faster way for a bidder to effect a takeover if the “offer is straightforward, no competing offer emerges and the bidder only needs to obtain ... 50 per cent ownership of the target”.²³⁴ At the very minimum an offer will take 44 days, assuming that the offer goes

²²⁷ Takeovers Code, r 43B(b).

²²⁸ See r 24(2)(b); rr 24A-24C; and Takeovers Act 1993, s 32(4)(d).

²²⁹ Overseas Investment Act 2005, sch 1 pt 1; and Overseas Investment Act, section 13.

²³⁰ Land Information New Zealand “Case 201520058 – JBS Australia Pty Limited” <www.linz.govt.nz>.

²³¹ See Scott Technology Limited *Scott Technology Ltd Scheme Booklet* (30 October 2015).

²³² See Takeovers Panel “Scott Technology Limited” <www.takeovers.govt.nz>.

²³³ Takeovers Code, r 25(3A).

²³⁴ Payne, above n 21, at 96.

unconditional during the offer period, from when the bidder gives notice to the target to when it goes unconditional, that is, a minimum of 14 days between giving notice of the offer and sending the offer to target shareholders and 30 days for the offer to remain open.²³⁵ Whereas, because of the need to “fit in two court hearings and [shareholder] meetings to vote on [a] scheme” it may be more difficult to complete a scheme as quickly as an offer.²³⁶ If speed in effecting a takeover is important to the bidder and the bidder is only seeking majority control of the target rather than 100 per cent control, an offer may arguably be the better mechanism. However, a scheme may still be faster if the bidder is seeking 100 per cent control. This is because once a scheme is approved, the bidder will have certainty of acquiring 100 per cent control, compared to under an offer, where the bidder will need to rely on the compulsory acquisition rules “to acquire the rump 10 per cent” of voting rights, under a process that “can add ... substantial delay”.²³⁷

D Bearing the Cost of the Takeover

The issue of who will bear the costs associated with a takeover may also make a scheme more attractive to a bidder. This is because the CA does not dictate who is to bear the costs associated with a scheme, therefore, it follows that each party to a scheme is to bear their own costs. However, recent scheme examples show that it is common for the issue of costs to be negotiated and determined during the development of the scheme. For example, in the takeover of Fliway Group Limited (Fliway) by Yang Kee Group (New Zealand) Pty Limited (Yang Kee) by way of a scheme, the issue of costs was agreed prior to the scheme being put to shareholders. Fliway and Yang Kee agreed, for example, that Yang Kee would pay Fliway “NZ\$200,000 as an initial contribution to Fliway’s transaction fees and costs” as well as a maximum amount of NZ\$60,000 to go toward the legal costs for preparing the scheme documentation.²³⁸

In contrast, under an offer, the bidder may be required to bear the full costs of the takeover. While the Panel encourages “parties to deal with the question of costs through negotiation”, the TA provides a procedure for the reimbursement of costs, to the target by the bidder, associated with a takeover offer.²³⁹ Under this process, the Panel can make a number of determinations for reimbursement of costs by the target to a director of the target and by

²³⁵ Takeovers Code, r 24(2)(b); r 43; and r 43B.

²³⁶ Payne, above n 21, at 96.

²³⁷ Payne, above n 21, at 96.

²³⁸ Fliway Group Limited, above n 139, at 29.

²³⁹ Takeovers Panel *Guidance Note on the Process for Costs Reimbursements under the Takeovers Act 1993* (21 March 2017) at [3].

the bidder to the target company.²⁴⁰ For example, the Panel can make a determination that a director of the target “is ... to be reimbursed by the target company for any expenses ... incurred by the director ... in relation to [an] offer or takeover notice”.²⁴¹ Additionally, the target “is entitled to be reimbursed by” the bidder “for any expenses ... incurred by the target company in relation to [an] offer or takeover notice” which may include the expenses incurred by the target when reimbursing a director.²⁴²

Therefore, it may be more appealing for the bidder to use a scheme so that the issue of costs can be determined in advance rather than taking the risk, under an offer, that they will need to reimburse the target an amount for costs that is uncertain until after the takeover is completed. However, in practice it is rare that any issue in relation to costs escalates to the point of requiring the Panel’s intervention. At the time of writing, there has only been one example where a dispute around payment by the bidder for expenses incurred by a target reached the Panel.²⁴³ In that case, although a Panel meeting was held to discuss a possible breach of the Code in relation to the unpaid expenses a settlement was reached between the bidder and the target prior to the meeting.²⁴⁴ As a result, the Panel made no determination as to whether the Code was breached.²⁴⁵

E An All or Nothing Mechanism

By their nature, schemes are an all or nothing deal structure.²⁴⁶ Regardless of whether some shareholders vote in favour of a scheme, if the required approval thresholds are not met (75 per cent of each interest class entitled to vote and voting on the scheme and a simple majority of the votes of those shareholders entitled to vote) the scheme will fail.²⁴⁷ Similarly, even if a scheme is approved by shareholders, if the court does not make an order to approve the scheme, it will fail.²⁴⁸ In contrast, the outcome of a takeover offer is not as black and white (as was discussed above in relation to certainty in the outcome of the takeover) because once the 50 per cent threshold is crossed there can be varying degrees of success which result in the bidder holding somewhere between 50 and 100 per cent control

²⁴⁰ Takeovers Act, s 50.

²⁴¹ Takeovers Act, s 48.

²⁴² Takeovers Act, s 49.

²⁴³ Takeovers Panel “Abano Healthcare Group Limited – 30 June 2008” <www.takeovers.govt.nz>.

²⁴⁴ Takeovers Panel, above n 243.

²⁴⁵ Takeovers Panel, above n 243.

²⁴⁶ MinterEllisonRuddWatts “Takeover Offer v Scheme of Arrangement – Structuring a friendly acquisition” (19 July 2018) <<https://minterellison.co.nz>>.

²⁴⁷ Companies Act, s 236A(4).

²⁴⁸ Companies Act, s 236(1).

of the target. A scheme, by comparison, will either succeed or fail which is an arguably a disadvantage to schemes over takeover offers.

1 Voting agreements and statements of voting intention

However, much like lock-up agreements assist a bidder to increase the certainty of the outcome and success of an offer, voting agreements and statements of voting intention can mitigate the risk of a scheme failing due to an insufficient level of shareholder support.

A voting agreement is an agreement between the bidder and a target shareholder that the shareholder will vote a certain way on the proposed scheme. Voting agreements arguably confer on the bidder “an element of” indirect control over a shareholder’s voting rights because the shareholder is exercising their voting rights in accordance with the bidder’s wishes.²⁴⁹ Shareholders subject to voting agreements may also be treated as associates of the bidder because of this element of control.²⁵⁰ However, the Panel have stated that “a voting agreement ... will not, on its own, result in an assumed association between the parties” and the “Panel will assess whether the terms of a voting agreement may give rise to a potential association ... on a case-by-case basis”.²⁵¹ Nevertheless, the arguable control over voting rights and possible association causes voting agreements to generally only be used “for up to 20 [per cent] of the target’s voting rights” so the fundamental rule is not breached.²⁵² A voting agreement can be contrasted to a lock-up agreement because a under lock-up agreement a shareholder is agreeing to accept the bidder’s offer to acquire their shares rather than agreeing to use their voting rights in a certain way.

A voting intention, on the other hand, is a “public statement” made by a target shareholder that declares their intention to vote to approve the scheme.²⁵³ Where a statement of voting intention is made by a shareholder, the Panel treats the statement as “a ‘last and final’ statement by the ... shareholder” which therefore, requires the shareholder to vote in accordance with the statement.²⁵⁴

Statements of voting intention, as opposed to voting agreements, may be preferable for the bidder because shareholders who have entered into voting agreements may also be required

²⁴⁹ Takeovers Panel, above n 14, at [2.27].

²⁵⁰ See Takeovers Panel, above n 14, at [2.29].

²⁵¹ Takeovers Panel, above n 14, at [2.29].

²⁵² Bell Gully, above n 33, at [17].

²⁵³ Takeovers Panel, above n 14, at [2.27].

²⁵⁴ Bell Gully, above n 33, at [17].

to vote on the scheme in a separate interest class which may have the reverse of the intended effect for the bidder.²⁵⁵ This is because, if all the shareholders who have, in advance, agreed to vote to approve the scheme are in a separate interest class, their votes to approve the scheme will be counted separately to all other shareholders which may magnify the impact of the votes any dissentient shareholders in another interest class. However, much like the issue of potential association, the Panel will “assess voting agreements on a case-by-case basis” in terms of determining whether shareholders subject to a voting agreement need to vote in a separate interest class.²⁵⁶ In contrast, statements of voting intention are “unlikely to result in the Panel forming the view that the shareholder should vote in a separate interest class”.²⁵⁷

The impact of a statement of voting intention can be illustrated by examining the recent takeover of Fliway by Yang Kee by way of a scheme.²⁵⁸ In this takeover, Fliway’s majority shareholder, who held 54.15 per cent of Fliway’s shares, made a statement of voting intention confirming that they intended to vote in favour of the scheme.²⁵⁹ When the scheme was voted on by shareholders, it was approved by 99.19 per cent of the votes cast by shareholders entitled to vote and voting and by 68.42 per cent of the total number of votes of those shareholders entitled to vote.²⁶⁰ If, at the shareholder vote, only the majority shareholder had voted in favour of the scheme and the same number of votes were cast against it, the scheme would still have been approved by a 98.9 per cent majority of the votes cast, and by a 54.15 per cent majority of the total number of votes of those shareholders entitled to vote.²⁶¹ However if, for any reason, the majority shareholder had been excluded from the vote, the scheme would have met the first voting threshold at 96.25 per cent approval but the scheme would have failed at the next threshold, receiving approval from only 31.13 per cent of the total number of votes of the shareholders entitled to vote.²⁶² This example shows that the statement of voting intention almost guaranteed that the scheme would succeed and that without the approval of the majority shareholder the scheme would have failed. Therefore, while a scheme is an all or nothing structure, the use of statements of voting intention, and voting agreements involving up to 20 per cent of

²⁵⁵ Takeovers Panel, above n 14, at [2.28].

²⁵⁶ Takeovers Panel, above n 14, at [2.28].

²⁵⁷ Takeovers Panel, above n 14, at [2.28].

²⁵⁸ *Re Fliway Group Ltd*, above n 17.

²⁵⁹ *Re Fliway Group Ltd*, above n 17, at [1]; and *Fliway Group Limited*, above n 139, at 29.

²⁶⁰ *Re Fliway Group Ltd*, above n 17, at [16].

²⁶¹ See *Re Fliway Group Ltd*, above n 17, at [16].

²⁶² *Re Fliway Group Ltd*, above n 17, at [20].

the voting rights, can mitigate the risk that the scheme will not receive sufficient shareholder support.

F Only Applicable to Friendly Takeovers

Another arguable disadvantage to schemes, when compared to takeover offers, is that they can generally only be used “to effect an agreed or friendly transaction”.²⁶³ This is because the “scheme process is controlled by the target rather than the bidder” and success of the scheme is reliant on the bidder working with the target board to negotiate and arrange the scheme before it is proposed to the target shareholders.²⁶⁴ Typically it is the target company board who will make the application to the court to consider the scheme and ultimately be responsible for it, however, it is theoretically possible for the bidder, if the bidder was already a shareholder of the target, to propose a hostile scheme without needing the target board’s involvement.²⁶⁵ This is because a scheme application can be made to the court by either the company or any shareholder.²⁶⁶

While in New Zealand there are no cases where the scheme process has been used by a bidder, who is also a shareholder in the target, to launch a hostile scheme, overseas cases highlight the difficulty of using a scheme in this way. For example, in the case *Re Savoy Hotel Ltd* it was confirmed that while the court may have “discretion to direct that meetings be held” to discuss a proposed scheme, “the court does not have jurisdiction to sanction a scheme that does not have the approval of the company”.²⁶⁷ In light of this, it is likely that where a scheme proposed by a shareholder “will not secure the approval of the company” the court will not use their discretion and “will not convene meetings”.²⁶⁸ Therefore, where the bidder is not able to gain the support of the target company for a proposed takeover, a scheme is not an available mechanism and the takeover would need to proceed as an offer.

1 Due diligence

However, the friendly nature of a scheme is arguably an advantage when the issue of due diligence is considered. Under a scheme, questions of “due diligence will usually arise ... as part of the ... negotiations in advance of proceeding with a scheme”.²⁶⁹ Whereas, under an offer, any due diligence conditions need to be carefully drafted so not to “depend on the

²⁶³ Payne, above n 21, at 102.

²⁶⁴ Payne, above n 21, at 102.

²⁶⁵ Payne, above n 21, at 102.

²⁶⁶ Companies Act 1993, s 236(1).

²⁶⁷ *Re Savoy Hotel Ltd* [1981] Ch 351 at 366; and Payne, above n 21, at 103.

²⁶⁸ Payne, above n 21, at 103.

²⁶⁹ Takeovers Panel “Offer Documents and Variations” (20 June 2017) <www.takeovers.govt.nz> at [4.32].

judgement” of the bidder as a condition of this kind would breach the Code.²⁷⁰ For example, a “due diligence condition that required the [bidder] to be ‘satisfied’ with the outcome of the due diligence would amount to a condition that depends on the judgement” of the bidder and would not be allowed.²⁷¹ In addition, because “due diligence includes the release of confidential financial and other information” to the bidder, the target “may ... refuse ... due diligence, particularly if the [bidder] is a potential competitor of the target”.²⁷² The Panel have confirmed that “refusal by the target ... to provide information” that goes “beyond the target board’s ... obligations to disclose information (such as ... under the NZX Listing Rules)” or as required by the Code “does not constitute a [prohibited] defensive tactic”.²⁷³ Therefore, if a due diligence condition is included in an offer, and the target board refuse “to provide the information, then the [bidder] may choose to rely on the condition and allow the offer to lapse” causing the takeover to fail.²⁷⁴

Therefore, although schemes are only applicable to friendly takeovers, there is an upside for the bidder to this friendly nature in that the bidder will be able to complete due diligence much more easily than under an offer.

G Splitting Shareholders into Interest Classes

While arguably not a disadvantage, the requirement under the CA for shareholders to vote on and approve a scheme with a 75 per cent majority “in each interest class” of shareholders,²⁷⁵ “makes schemes potentially more cumbersome” because the splitting of shareholders into interest classes is not required for a takeover offer.²⁷⁶ The need for shareholders to vote in interest classes may also be a disadvantage for the bidder because the more interest classes there are, the higher the risk will be that the 75 per cent approval threshold requirement will not be met in each interest class which would cause the takeover to fail. Therefore, the bidder “will usually desire to have fewer interest classes”.²⁷⁷

Additionally, incorrectly splitting shareholders into interest classes may be fatal for a scheme because it may lead to the results of the shareholder vote on the scheme incorrectly representing the level of support the scheme received. If the court is not satisfied that “the

²⁷⁰ Takeovers Panel, above n 269, at [4.34]; and Takeovers Code, r 25(1).

²⁷¹ Takeovers Panel, above n 269, at [4.35].

²⁷² Takeovers Panel, above n 269, at [4.37].

²⁷³ Takeovers Panel, above n 269, at [4.39].

²⁷⁴ Takeovers Panel, above n 269, at [4.40].

²⁷⁵ Companies Act 1993, s 236A(4)(a).

²⁷⁶ Payne, above n 21, at 108.

²⁷⁷ Takeovers Panel “Code Word 42” (October 2016) <www.takeovers.govt.nz>.

scheme has been fairly put to the ... classes concerned”, at the final hearing, the scheme may not be approved by the court.²⁷⁸ Fortunately, to mitigate this risk, prior to the initial court hearing, regardless of whether a no-objection statement has been applied for, the Panel will have reviewed the proposed identification of interest classes and will have either provided a letter of intention to indicate that the Panel believes the interest classes have been adequately identified or the Panel will likely seek to be heard at the first court hearing on the issue of interest classes.²⁷⁹ The court in the initial hearing will also make a direction as to the determination of shareholder interest classes prior to the shareholder vote.²⁸⁰ Therefore, the bidder can be assured that the Panel and the court will ensure interest classes are adequately identified.

H Conclusion

Part VI of this paper has explored the bidder’s choice to effect a takeover as either a scheme or as an offer by comparing the advantages and disadvantages of both mechanisms. It is submitted, as a result of this comparison, that while there are arguable advantages and disadvantages to both mechanisms, the choice provides “economically sensible commercial flexibility” because both are capable of achieving equally successful outcomes for the bidder.²⁸¹

VII Potential for Reform

Through the analysis and discussion in this paper, there is one aspect of the scheme process that stands out as a potential area for further reform, that is, the need for two court hearings for a scheme to be approved. This paper submits that there is an opportunity to reform the CA by legislating for any procedural matters, in relation to a scheme that involves a code company, that are currently addressed the first hearing. Legislating for any procedural matters would remove the need for a first court hearing which would make the scheme process more efficient.

Prior to 2014, the first court hearing was necessary because the court was required to exercise “vast discretion” to determine the procedural steps for a proposed scheme (as discussed in Part IV of this paper) because the legislation provided “no guidance” on the scheme process.²⁸² As result of the 2014 changes to the CA and the increased use of

²⁷⁸ *Re Nuplex Industries* [2016] NZHC 1677, at [10].

²⁷⁹ Takeovers Panel, above n 14, at [3.4]; and Takeovers Panel, above n 14, at [2.4].

²⁸⁰ See Companies Act 1993, s 236(2)(b).

²⁸¹ Takeovers Panel, above n 14, at [1.5].

²⁸² Clune, above n 36, at 100.

schemes to effect takeovers, it is arguable that the need for court discretion in the first court hearing is no longer necessary because the law surrounding schemes relating to code companies is now relatively settled. However, the legislation still lacks a clear process for schemes. This means that, the court in the first hearing, without needing to exercise much discretion, is still required to make orders on matters such as, who must be notified of a proposed scheme, who is entitled to appear and be heard on a scheme application in the final court hearing, on the make-up of shareholder interest classes, on the information to be provided to shareholders and when this information must be provided as well as, ordering meetings of shareholders in interest classes to consider and vote on the scheme and when these meetings must be held.²⁸³ The remainder of Part VII of this paper touches on each of the above procedural matters and explains why they no longer require court discretion before briefly suggesting how the CA could be reformed to provide an alternative to requiring a first court hearing.

A Who Must be Notified

Given the increased use of schemes there is now clear precedent on who must be notified of a scheme application. Recent cases show that the target shareholders, directors and auditors must all be notified of the scheme and an advertisement announcing the proposed scheme must be run in all “major daily newspapers”.²⁸⁴ In light of this, there is arguably no court discretion required on who must be notified of a proposed scheme, therefore, a provision could be inserted into the CA to cover this requirement.

B Who is Entitled to Appear

Similarly, recent scheme cases show there is also a clear precedent on who is entitled to appear and be heard on the proposed scheme in the final court hearing. The Panel, bidder, target company, target company shareholders and “any other person who considers they have a proper interest in the Scheme and who wishes to appear” are all able to appear and be heard at the final court hearing.²⁸⁵ Therefore, again, there is no court discretion required and a provision could be inserted into the CA to the above effect.

C Determination of Interest Classes

Historically, “one of the key issues” for the court at the first hearing was deciding whether shareholders “should be split into separate classes for the purpose of voting on the

²⁸³ Companies Act 1993, s 236(2).

²⁸⁴ *Re Nuplex Industries*, above n 171, at [14]-[15] and [22]; and *Re Fliway Group Ltd* HC Auckland CIV-2017-404-2704, 20 November 2017 at [14]-[15] and [22].

²⁸⁵ *Re Nuplex Industries*, above n 171, at [25]-[27]; and *Re Fliway Group Ltd*, above n 284, at [25]-[27].

scheme”.²⁸⁶ While the court in the initial hearing still comment on the make-up of shareholder interest classes it is arguable that this is no longer an exercise of the court’s discretion.²⁸⁷ The court’s discretion is no longer required because, as discussed in Part IV of this paper, the Panel, review all proposed schemes (regardless of whether a no-objection statement has been applied for) and form a view on the determination of interest classes. Additionally, as part of the 2014 reform of the CA, a new schedule was inserted into the CA for the purpose of providing guidance on the determination of interest classes for schemes that involve a code company.²⁸⁸ Therefore, so long as interest classes are determined in accordance with sch 10 of the CA and the Panel confirm they are satisfied with the determination of interest classes, there is arguably no court discretion required. However, because no-objection statements are not mandatory, a provision would likely need to be inserted into the CA that would require a no-objection statement to be gained in place of the first court hearing to ensure that interest classes have been adequately determined.²⁸⁹

D Information to be Provided to Shareholders

The Panel also review any documents relating to a proposed scheme (again, regardless of whether a no-objection statement has been applied for) to ensure that “all material information ... has been disclosed” to shareholders and that “the standard of disclosure ... has been equivalent to the standard required by the Code”.²⁹⁰ Therefore, so long as the Panel has reviewed any scheme documentation and are satisfied with the level of disclosure, there is arguably no court discretion required. Additionally, given the increased use of schemes to effect takeovers, it is also arguable that there is now a clear precedent contained in the initial orders from recent scheme cases that could be used as a basis for information disclosure in future scheme cases.²⁹¹ It is submitted that additional provisions could to be inserted into the CA, based on these recent scheme cases to clearly set out exactly what information must be provided to shareholders. It is also submitted that any new provisions could be in a similar form to the schedules of the Code that deal with the content of any offer documents to create consistency between the Code and the CA in relation to disclosure requirements.²⁹² A no-objection statement would also need to be

²⁸⁶ Payne, above n 21, at 36.

²⁸⁷ See *Re Nuplex Industries*, above n 171, at [6]; and *Re Fliway Group Ltd*, above n 284, at [6].

²⁸⁸ Companies Act 1993, sch 10.

²⁸⁹ See Companies Act 1993, s 236A(2)(b)(ii).

²⁹⁰ Takeovers Panel, above n 14, at [3.4].

²⁹¹ See for example, *Re Nuplex Industries*, above n 171, at [14]; and *Re Fliway Group Ltd*, above n 284, at [14].

²⁹² See Takeovers Code, schs 1 to 3.

mandatory, in place of an initial court hearing, to ensure that the Panel are satisfied the standard of disclosure is adequate.

E Shareholder Meetings

As a result of the 2014 changes, any scheme that involves a code company, requires shareholder approval by way of a vote on a resolution proposing the scheme.²⁹³ The CA now also specifies the voting majorities required to pass the resolution that proposes the scheme.²⁹⁴ Therefore, where the court previously had to exercise discretion as to the extent to which meetings were required and the voting majorities required to approve a scheme, this discretion is no longer required. However, the court, in the initial hearing, are still required to order meetings of shareholders to be held because the CA does not specify that meetings must be held, only that the shareholders must vote to approve the scheme. In the absence of a court order requiring meetings of shareholders to be held, it is submitted that, provisions could be inserted into the CA to the effect that shareholders must meet in their respective interest classes to consider and vote on a proposed scheme.

F Timeframes

To ensure that shareholders have “adequate time to make their decision” whether to approve or reject a proposed scheme, the court in the initial hearing, must also make orders as to when information relating to the scheme is to be provided to shareholders and also when shareholder meetings must be held.²⁹⁵ It is arguable that in making these orders the court are no longer required to exercise their discretion because recent scheme cases have set a precedent for these timeframes.²⁹⁶ Recent scheme cases show that shareholders are required to be provided with the information relating to a scheme at least 10 days before the shareholder meetings are held.²⁹⁷ However, because the CA is currently silent on any timeframes for schemes, provisions would need to be inserted into the CA to specify the minimum timeframes that shareholders must have to consider the proposed scheme before voting whether to approve it if an initial court hearing was not held.

G Shareholder Protection

Finally, it is important to consider whether shareholders are still adequately protected if the need for an initial hearing was removed and the CA was reformed to provide a process for

²⁹³ Companies Act 1993, s 236A(2)(a).

²⁹⁴ Companies Act 1993, s 236A(4).

²⁹⁵ Takeovers Panel, above n 58, at 6; and Companies Act 1993, s 236(2)(a)-(b).

²⁹⁶ See for example, *Re Nuplex Industries*, above n 171, at [15]; and *Re Fliway Group Ltd*, above n 284, at [15].

²⁹⁷ *Re Nuplex Industries*, above n 171, at [15]; and *Re Fliway Group Ltd*, above n 284, at [15].

schemes involving code companies. It is submitted that removing the initial hearing, and implementing the suggested reform discussed above, does not negatively affect any of the shareholder protections that were discussed in Part V of this paper. This is because shareholders would still be required to vote on a proposed scheme in interest classes, the requisite voting majorities would remain unchanged, any person who wished to be heard on the scheme could still appear at the final hearing, the target company directors would still be subject to their duties as directors, any scheme documentation would still need to be prepared in alignment with the Code and most importantly the court would still have the ultimate decision on whether to approve the scheme.

VIII Conclusion

To conclude, in New Zealand, a bidder when launching a takeover, has the choice to effect the takeover as either a scheme or an offer. This paper has explored this choice by comparing the law relating to both mechanisms in light of the increasing use of schemes, under the CA, as an alternative to an offer, under the primary regulation relating to takeovers that is contained in the Code.

Parts I and II of this paper introduced and provided background on the rationale for the regulation of takeovers. Parts III and IV explained the law relating to takeover offers and schemes, which included an explanation of the process for effecting a takeover under both mechanisms. Part V of this paper considered whether shareholders are adequately protected when a takeover occurs by way of a scheme in comparison to the Code's paradigm of shareholder protection. Part V submitted that shareholders are sufficiently protected as the result of a number of additional protections that form part the scheme process. Part VI of this paper then discussed the advantages and disadvantages of a scheme when compared to a takeover offer to understand why a bidder may choose to structure a takeover as one over the other. As a result of this comparison, this paper submitted that while there are arguable advantages and disadvantages to both mechanisms, on balance, both are capable of producing a successful outcome for the bidder. Finally, this paper explored the potential to reform the CA to make the scheme process more efficient by removing the need for an initial court hearing. This was proposed because it has arguably become unnecessary for the court to exercise their discretion on any procedural matters relating to schemes in light of the reform of the CA in 2014 and a clear precedent that has emerged in recent scheme cases.