TAKEOVERS PANEL

Guidance Note on Independent Advisers and the Takeovers Code

1 March 2018

Introduction

1. The purpose of this Guidance Note is to assist those who are approved as independent advisers by the Panel to prepare a report under any of rules 18, 21, 22, or 57 of the Takeovers Code or under a class exemption or individual exemption granted by the Panel from the Code.

2. The Guidance Note is divided into the following parts:

   (a) General comments that apply in all cases;

   (b) Reports required in relation to takeover offers (reports under rules 21 and 22 of the Code);

   (c) Reports required in relation to meetings of shareholders (rule 18 of the Code, exemptions from the Code, and share buybacks); and

   (d) Reports required in relation to compulsory acquisitions under the Code (rule 57).

3. The Guidance Note has the following appendices:

   (a) Appendix A: The Panel's policy on the approval of independent advisers;

   (b) Appendix B: The information that must be provided to the Panel by a firm or individual (including subcontractors) applying to be approved to be an independent adviser; and

   (c) Appendix C: The statement of independence that must be included in the independent adviser's published report.

General comments

4. The Panel considers that the role of the independent adviser is critical to the effectiveness of the Code in regulating the market for the control of Code companies.

5. The independent adviser helps to ensure that shareholders are well informed when a takeover offer is made or another transaction occurs that requires shareholder approval under the Code. For this reason, the Panel takes a close interest in the competence as well as the independence of any firm or individual proposed for appointment as an independent adviser.

6. Advisers need to fully appreciate the philosophy of the Code, the rights it creates for shareholders, and the importance of the adviser's role in the process. Reports must be of a high quality and give balanced advice.

Role of the Takeovers Panel

7. A crucial piece of information for shareholders involved in Code-regulated transactions is provided by an independent adviser who reports on the merits of an offer or a proposed company transaction. Often a valuation will form part of the adviser's merits analysis.

Any valuation included in an independent adviser's report is fundamentally an opinion of the adviser, formed in its capacity as an independent expert.

8. A key part of the Panel's role is to ensure that the process requirements and information disclosure mandated by the Takeovers Code are met. The purpose of Code-mandated disclosure is to provide information which allows the Code company shareholders to decide for themselves whether to accept a takeover offer or to approve a Code-regulated transaction.

The Panel approves the appointment of the adviser

9. The Panel's role is to approve the appointment of an independent adviser appointed by a Code company. The Panel must be satisfied that the adviser is independent of all parties to a takeover or company transaction and competent to write the report. If so satisfied, the Panel will approve the appointment of the adviser, but thereafter the Panel's role is limited to enforcing the Code.

The Panel is not a 'merits' regulator

10. One of the principles of the Takeovers Code is that shareholders decide for themselves the merits of a takeover or company transaction. They make this decision with the benefit of advice from the company's directors and from an independent adviser that is appointed by the company's directors (or a committee of the independent directors) and approved by the Panel.

11. The Code does not set the Panel up to be a 'merits' regulator. The Panel does not stand in the shoes of the shareholders to decide what is best for them.

12. Accordingly, the Panel is not required to, and does not, consider the merits of an independent adviser's opinion. This means that the Panel does not review or comment on the valuation methodology used in an independent adviser's report or on the valuation conclusion reached by the independent adviser.

13. The Panel has an enforcement role to ensure that no person engages in conduct in respect of a takeover or other Code-regulated transaction that is misleading or deceptive, or likely to mislead or deceive. This prohibition on misleading or deceptive conduct (rule 64 of the Code) applies to every person, including to independent advisers.

14. The legal test that would be applied to determine whether an opinion expressed by an independent adviser or other person was misleading or deceptive is as follows:[1]

    (a) was the opinion honestly held?

    (b) was the opinion reasonably based? and

    (c) was the opinion demonstrably wrong?

[1] For a review of how the Panel has applied this legal test to an opinion expressed by directors of a target company, see the determination of March 2010 in the matter of Horizon Energy Distribution Limited at paragraphs 134-143.

15. Shareholders, target company directors and advisers may complain that a valuation is flawed, for example, where the valuation methodology used is a discounted cash flow analysis and the complaint alleges that the discount rate applied is wrong or the comparatives on which the multiples have been taken are inappropriate. The Panel will not entertain complaints of this nature, which are simply an expression of opinion, unless the legal test for misleading or deceptive conduct is met.

16. The Panel considers that an independent adviser's report will include a valuation involving the adviser's own expert opinion. Although another expert might hold a differing opinion, in the field of valuation there may be a broad range of views amongst equally competent experts as to value.[2] Accordingly, an independent adviser's report will not breach rule 64 of the Code unless the legal test for misleading or deceptive conduct is met.

Role of the Code company's directors

17. The independent directors of the Code company also have important responsibilities in the process. The Panel believes, on the basis of some of the reports it has seen, that not all independent company directors have appreciated the extent of those responsibilities.

18. The directors need to ensure that the appointed adviser is given all the information necessary to provide a comprehensive and accurate report. They should, in the course of reviewing the independent adviser's draft report, satisfy themselves that it is sufficiently comprehensive, is factually accurate, and covers all the relevant issues. However, the Panel expects directors to form their own view on the offer when making their recommendation (see paragraphs 39 to 43 of the Panel's Guidance Note on Target Company Statements).

Review of draft reports

19. One of the Panel's primary responsibilities is to approve independent advisers. It is a normal condition of the Panel's approval of an independent adviser to require a draft version of the report to be sent to the Panel at the same time it is provided to the directors of the Code company for factual review. The Panel will continue its policy of reviewing reports in draft and will provide comments to the advisers where it considers this is appropriate.

Clear, concise and effective independent adviser reports

20. The Panel expects a user-friendly independent adviser's report for shareholders. Drafting should follow a clear and concise style, with minimal use of jargon and repetition, and plain English used where possible. If information is summarised, a balanced view of any advantages and disadvantages should be provided.

21. More specifically, an independent adviser's report should be:

    (a) Clear:

        (i) use plain language;

[2] Horizon Energy Distribution Limited determination, paragraph 142

(ii) use a font and font size that are easily readable;

(iii) be logically ordered and easy to navigate;

(iv) highlight important information; and

(v) explain complex information in plain language and include a clear explanation of any necessary jargon;

(b) Concise:

(i) use short sentences;

(ii) avoid unnecessary repetition;

(iii) highlight important information in balanced summaries, including a summary of the adviser's conclusions on the merits of the transaction near the front of the report;

(iv) use diagrams and graphs effectively; and

(v) minimise the use of brand information, photographs and other images;

(c) Effective:

(i) give adequate and accurate information about the transaction; and

(ii) convey an accurate and balanced impression.

Disclosure of principal assumptions underlying forecasts

22. Independent adviser reports will ordinarily set out prospective financial information, comprising financial forecasts of the target company for one or more years, as it could reasonably be expected to be material to the decision of offerees to accept or reject an offer. Prospective financial information usually comprises forecasts that are based on information provided by the company appointing the independent adviser.

23. The Code requires an independent adviser's report to state the principal assumptions on which any prospective financial information is based. The Panel expects that the assumptions will directly accompany the relevant prospective financial information in the document and be set out in a way that is helpful and relevant for shareholders reading the report.

24. Prospective financial information will usually be based on many assumptions about future conditions and events which may or may not occur. The quality of the information will be dependent largely on the appropriateness of the assumptions. Providing shareholders with these assumptions assists them to make their own informed judgement on the quality and reliability of the information.

25. Assumptions can range from being reasonably certain to very uncertain. In setting out assumptions in a useful and relevant way, it is likely to be helpful to address, among other things:

(a) the degree of certainty/risk associated with particular assumptions and the key factors that could cause them to be incorrect;

(b) the extent to which assumptions relate to matters within or outside the control of the entity; and

(c) source material that has been used in deriving assumptions (e.g. past performance, third party reports or research, other market data).

26. For shareholders to make their own informed judgement, it may also be necessary to provide information which assists them in assessing the sensitivities of prospective financial information, where appropriate (for example, where there may be significant risks that could render those assumptions invalid and therefore alter key financial information and impact valuation or merits).

27. In determining what information to provide, the key question is whether it could reasonably be expected to be material to the making of a decision by the offerees to accept or reject the offer.

Reports for takeover offers

28. The Code requires independent advisers' reports to be prepared for the offerees in all takeover offers made under the Code. In every case, a report obtained by the directors of the target company under rule 21 of the Code is required to accompany the target company statement. In some cases, where full or partial offers have been made and there is more than one class of equity security (full offers) or more than one class of voting security (partial offers), an additional report under rule 22 of the Code is required (obtained by the offeror) to certify the fairness and reasonableness of the consideration being offered as between different classes of equity security.

29. Some observations about the requirements of these various reports are set out in the next section of this Guidance Note. In all cases, the adviser needs to ensure that it has a thorough knowledge of how the relevant rules of the Code work.

<u>Rule 21 reports on the merits of a takeover offer</u>

Full offers

30. The report should include a valuation exercise that compares the consideration being offered by the offeror against various measures of the value of the target company. Questions the adviser could address, among others, include:

(a) If the offer is a cash offer, is it worth more to the target company shareholder to stay in the company or to realise his or her or its investment for the price offered? What are the key valuation judgments that support this view?

(b) If the offer is a scrip offer, what is the value and the prospects of the entity whose securities are being offered, against the value and the prospects of the target company?

(c) Is it appropriate to include a premium for control? Does the offeror already have effective or legal control of the target company?

31. The Panel recommends that advisers should not describe offers as "fair" or "unfair". A comparison of the offer price with the adviser's valuation should probably be made, but this is only one of a number of issues that the adviser may usefully discuss in its report on the merits of the offer.

32. One exception to this recommendation is where the primary purpose of the report is to provide guidance to shareholders who are certain, or at least very likely, to have their shares taken under compulsory acquisition as the result of an offer. In such cases it may be appropriate for the adviser to express a view on the "fairness" of the offer price.

33. An important issue for the adviser in preparing valuation material would be the reliance it should place on any forecast financial information available from the target company. This in turn could have a significant bearing on the quality of its final report. Issues that the adviser may need to consider could include, among others:

    (a) the extent to which the adviser should rely on forecasts of future financial performance prepared by the target company;

    (b) whether the adviser should carry out its own "reasonableness tests" of prospective financial information provided by the target company before using that information in its report and any valuation it undertakes;

    (c) whether the adviser should prepare its own financial forecasts for the target company based on its own analysis, but using source data from the target company; and

    (d) the time period over which any forecast financial information does or should extend.

34. It is also important that the adviser have regard to any applicable professional standards. The Panel draws advisers' attention to Advisory Engagement Standard No 2 *Independent Business Valuation Engagements* ("AES–2") issued by the Institute of Chartered Accountants of New Zealand in 2001, and effective for all valuation engagements undertaken by members of the Institute from 1 April 2002. However, advisers should always be mindful that reports under the Code are not simply valuations, but are reports on the merits of an offer.

35. If there is any collateral arrangement with one or more, but not all, shareholders of the target company in conjunction with the offer this is likely to raise the issue of the offer's compliance with rule 20 of the Code. Rule 20 states that an offer must be on the same terms and provide the same consideration for all securities belonging to the same class of equity securities under offer.

36. The Panel expects advisers, as part of their assessment of the merits of any particular offer to investigate and to comment in their reports on the reasonableness of the terms and conditions of any collateral arrangement. The Panel will take into account the adviser's views when considering whether the offer complies with the Code.[3]

37. The adviser should comment on the position of the offerees if they opt not to accept the offer. These comments could cover, among others, matters such as:

[3] Please refer to the Guidance Note on Rule 20 and Collateral Arrangements

(a) whether, if the offer is conditional on the offer reaching 90%, this condition can be waived at the discretion of the offeror;

(b) the prospects of the offer consideration being increased;

(c) the position of minority shareholders if the offer falls short of 90% acceptance, and/or the offeror waives any 90% condition that may have been part of the offer. for example:

(i) could they be left as part of a small minority of shareholders, with an illiquid stock?

(ii) how may remaining minority shareholders be affected by the offeror's plans for the target company once it has control?[4] Might these plans add value to the company in the near or longer term?

(iii) how does the offeror propose to deal with conflicts of interest if it is a competitor of the target company and could now also be the major shareholder of the target company?

38. The adviser may need to comment on the options available to the offeror under the Code if it reaches, or does not reach, the compulsory acquisition threshold. These comments could cover such matters, among others, as:

(a) the ability of the offeror to subsequently acquire sufficient shares through "creeping" under rule 7(e) to reach that threshold. If so, the adviser should note that "creeping" is not possible until after twelve months from the conclusion of the offer period; and

(b) the rights and obligations of the remaining minority shareholders under a compulsory acquisition (see Part 7 of the Code).

39. The situation of competing offers may also need to be addressed. The adviser's comments could cover such matters, among others, as:

(a) the likelihood of competing offers emerging if there are no known competing offerors;

(b) a comparison of competing offers with the offer that is the subject of the report. What is the likelihood of the offer consideration of one offer or the other being increased?

(c) statements that may have been made by the parties as to their intentions. (In this regard advisers should bear in mind the provisions of rule 64 of the Code relating to the prohibition on misleading or deceptive conduct in takeovers.);[5] and,

(d) the effects of the timing rules of the Code on the competition for control of the target company. When should an offeree accept one offer or the other?

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[4] The offer documents for all takeover offers under the Code (except those which contain a non-waivable 90% minimum acceptance condition) must contain a statement of the offeror's intentions in respect of material changes to the target company: see clause 14, Schedule 1 of the Code.

[5] The Panel's Guidance Note of Rule 64 of the Code.

Partial takeover offers

40. With a partial offer, the offeror must stipulate the percentage of the securities that it does not hold for which it is bidding. This is the "specified percentage". Other than under the procedure described in the following paragraph, partial offers must have a minimum acceptance level of more than 50% of the voting rights in the target company and must obtain at least that percentage in order for the offer to be able to be successful. If acceptances fall short of the minimum acceptance percentage, the offer will fail. If acceptances exceed the specified percentage, they will be scaled back. In some cases, shareholders may be successful in selling all their holdings into a partial offer but a more realistic assumption may be that current shareholders will be left with some shares in the target company.

41. If the offeror is seeking to acquire shares in the target company that would increase its control percentage to between 20% and 50% of the total voting rights, the offer must be approved by a majority of the shareholders of the target company not associated with the offeror that vote on the proposal.[6] This voting process takes place during the offer period.

Accepting or rejecting the offer

42. The merits of the partial offer are likely to include a valuation of the target company and, in the case of a scrip bid, of the offeror. The adviser would need to consider how to value a partial interest in the target company. This may depend on whether the offeror is seeking more than 50% of the voting securities or somewhere in the 20 – 50% range with shareholder approval.

43. Some of the same considerations may apply as in a full offer, but there are likely to be additional complexities with a partial offer. Comments could cover matters, among others, such as:

    (a) the reasons for a partial offer as opposed to a full offer;

    (b) having regard to the percentage of voting rights that the offeror is seeking to control, the benefits (and detriments) that may accrue to the company and the shareholders if that level of control is achieved by the offeror;

    (c) the prospects of shareholders being able to sell all or most of their shares into the offer, having regard to the scaling rules of the Code and the likelihood of success of the offer. This discussion may have added significance if there are competing partial offers, with competing offerors starting from different voting control positions; and

    (d) the timing implications of accepting partial offers.

44. In commenting on the merits of a partial offer, advisers should reflect on whether control considerations outweigh pricing issues as far as the impact on target company shareholders is concerned.

45. The adviser could discuss the consequences for shareholders who choose to accept, or not to accept, the offer. The consequences of not accepting the offer might include:

[6] The shareholders who are not eligible to vote are the offeror and its associates. If another shareholder is also making a takeover offer for the target at the same time it would be eligible to vote on the competing offer.

(a) if sufficient shareholders respond in the same way, the offer failing, or the offeror increasing its offer price or making a (later) full offer for all the equity securities in the company;

(b) any premium that is being paid by the offeror being paid to only the accepting shareholders;

(c) in the event that the partial offer succeeds, the accepting and non-accepting shareholders being left as minority shareholders in a company controlled by a single shareholder; and

(d) any other implications for the control of the company and the characteristics of its share register as a result of the offer.

46. The adviser should give some guidance in the report on the likely effects on the holdings of accepting shareholders if the acceptances of the partial offer are subject to scaling. The relevant provisions of the Code are in rules 12 to 14. The explanation should assist offerees to understand the number of their securities that could be taken up by the offeror.

47. The adviser may need to comment on any plans the offeror may have for the target company. These intentions should have been disclosed in the offer document if the offeror intends to make any material changes in respect of the business activities of the target company (clause 14, Schedule 1 of the Code). The adviser may comment on whether it considers the offeror will add value to the company over time. It may also be relevant to comment on how the offeror intends to deal with any conflicts of interest if it is a competitor of the target company. If the offeror will not provide the adviser with any information on these questions, the adviser may wish to comment accordingly.

48. Having regard to the Code, the adviser could also comment on future prospects for the remaining shareholders after a successful partial offer. These comments could cover matters, among others, such as:

(a) the controlling shareholder's "creep" rights under rule 7(e) of the Code (if it has control of over 50% of the voting rights) (see above);

(b) the likelihood of future takeover offers under the Code from the controlling shareholder, or from other offerors;

(c) having regard to the offeror's stated intentions for the target company if the offer is successful, the likelihood of enhancement to the value of target company shares for the minority shareholders as a result of increased financial or managerial support for the company from the new majority shareholder; and

(d) alternatively, the likelihood of detriment to the value of those shares in the event of diminished liquidity and a reduced possibility of future takeover activity following a successful takeover.

The right to vote for or against a partial offer

49. If the offeror is seeking to acquire a voting percentage between 20 and 50% of the target company, it can only do so with the approval of a majority of the votes of target

company shareholders not associated with the offeror. The Panel believes it is important that shareholders are well advised of the merits of voting for or against a partial offer made in that range.

50. The adviser may need to comment on the merits (or otherwise) of a shareholder increasing its holding to the 20 – 50% range without making an offer for more than 50% of the voting rights in the target company.

51. In addition, as with any offer, the offerees also have to decide whether to accept the offer itself. In making this decision, a shareholder has to take into account that, regardless of whether the shareholder votes for or against the offer, or chooses not to vote, the offeror could receive sufficient votes to make the offer in the 20 – 50% range. This is a complex situation, and one that advisers need to explain well to target company shareholders. Advisers should note that an amendment to the Code in 2013 means that the voting period closes seven days before the end of the offer period. Accordingly, the offerees have the opportunity to consider the outcome of the vote before they make a decision to accept or reject the offer.

52. The control outcome sought in the target company may be an important consideration in discussing the merits of the shareholders' choice whether to vote in favour of or against a partial offer for 50% or less control. Comments in the adviser's report could cover various matters, including:

    (a) the effect of the offeror obtaining the sought after percentage, say, 35% of the voting rights, in the target. To what extent is this holding expected to give the offeror effective control of the company?

    (b) the benefits that the offeror may bring to the company from an increased control percentage to justify the remaining non-associated shareholders voting to approve the percentage sought;

    (c) the reasons why a shareholder might vote to approve or not approve the offeror obtaining a stake in the 20% to 50% range;

    (d) the price being offered by the offeror; and

    (e) the likely effects of the offer, if accepted, on the shareholder's own shareholding, given the Code's scaling rules?

<u>Rule 22 reports – offers for multiple classes of securities</u>

53. Under rule 22 of the Code, an offeror must obtain –

    (a) a report from an independent adviser if rule 8(3) or 8(4) or 9(5) applies; and

    (b) a report or an amended report from an independent adviser, if rule 44(3) applies.

54. In the report, the independent adviser must certify that, in the adviser's opinion, the offer complies with rule 8(3) or 8(4) or 9(3) as the case may be.

55. If an independent adviser's report is obtained, the offer is deemed to comply with rule 8(3) or 8(4) or 9(5) as the case may be.

56. Rule 8 of the Code states that where a person is making a full offer for all the voting securities of a company, it must also make an offer for all the other classes of equity securities of the company. That offer must be "fair and reasonable" as between the various classes of equity securities.[7] In order to ensure that the offer satisfies this requirement, an independent adviser is required to certify that this is the case. Once the adviser has given this certificate then the offer is deemed to comply with the relevant rule. (Under rule 9 of the Code, dealing with partial offers, if there is more than one class of voting securities, similar provisions apply.) Schedule 3 of the Code prescribes the basic requirements for a report under rule 22.

57. The Code permits an offeror to revise the terms of its offer (without the prior approval of the target company's directors) to include classes of securities, or to take into account terms of a class of securities, of which the offeror was unaware at the time it sent a takeover notice. In order to be able to rely on the procedure under the Code for this, a rule 22 report or amended rule 22 report (relating to the added or changed classes of securities) has to accompany notification by the offeror to the target company, under rule 44(3), of the offer or offers for the added or changed class(es) of securities.

58. A rule 22 report is probably the narrowest of all in scope. It is not a report on the merits of the offer, but only on the relativity between the offers being made for each relevant class of securities. It is likely to be quite technical in nature, starting with the consideration being offered for the target company's primary securities, and then assessing the relationship between that price and the value of the consideration being offered for other relevant classes of security.

59. Issues that might arise in the report could include the conversion price that has to be paid to exercise any options or convertible notes in order for them to be converted into voting securities, and the period the options or conversion rights have to run.

60. Even if options are apparently worthless, because their exercise price exceeds current market value, the offeror under a full offer must still offer to purchase such securities. An assessment of the fairness of the price offered might include an assessment of the likelihood of the options having positive value in the future.

61. The Panel considers that the adviser should provide background analysis and commentary in the rule 22 report. It would not be sufficient for an adviser to simply issue a bare certificate that the offer was fair and reasonable as between the different classes of securities included in the offer.

Reports required for shareholder meetings

62. Under rules 7(c) and 7(d) of the Code, and also under the terms of some Panel exemptions, a report from an independent adviser on the merits of an acquisition or allotment affecting Code company voting rights must be provided to the shareholders entitled to vote on the relevant resolution. The acquisition or allotment may be of voting rights in the Code company or of securities in an upstream body corporate.

[7] The offer must be fair and reasonable as between classes of voting securities, and as between voting and non-voting securities, where applicable.

63. In each case, the shareholders (excluding the acquirer/allottee and its associates) are given the right by the Code to approve or reject proposals for another entity to increase its control percentage of the Code company. This right to approve should be exercised by the relevant shareholders with care and on the basis of good advice.

64. It is an important part of the adviser's role to ensure that shareholders are properly advised of their rights under the Code. For example, shareholders should be made aware that it is not necessary to approve a proposal simply because there are few negatives. Shareholders can vote against a proposal in order to allow the status quo to continue having taken into account reasons for and against that course of action.

65. Rule 18 of the Code requires the directors of the Code company to obtain a report from an independent adviser on the merits of any proposed acquisition under rule 7(c) or an allotment under rule 7(d) having regard to the interests of those persons who may vote to approve or disapprove the acquisition or allotment. Some of the main reports prepared for shareholder meetings conducted under the Code are discussed below.

Rule 18 reports – acquisitions (rule 7(c))

66. A rule 7(c) acquisition is one where the acquirer (together with any of its associates) will become the holder or controller of more than 20% of the voting rights in a Code company, (or, if the acquirer already holds or controls more than 20%, a higher percentage) from another party or parties. The acquisition may be of a Code company's shares, or it may be of the securities of another body corporate upstream of the Code company that controls voting rights in the Code company.

67. The independent adviser is not advising the parties to the transaction, but instead those who have the right to vote to approve or disapprove the acquisition. As such, valuation may or may not be the key issue.

68. The consideration for the transaction may be an issue if the acquirer is obtaining a controlling parcel of shares without making an offer to remaining shareholders. The price being paid could impact on the market value of the holdings of existing shareholders if the parcel is large enough. The adviser may address the question of whether the value of the voting shareholders' shares is likely to be affected by the level of consideration.

69. The shareholders of the Code company, other than the buyer(s) and the seller(s), must approve any changes in holdings of shares that increase the acquirer's holding or control[8] above 20%[9] unless the acquiring shareholder makes either a full or a partial offer for the target company in which all shareholders would have the right to participate.

70. Factors covered in a report might include, among others:

    (a) the prospects of the acquirer making a full or partial offer for the company if the shareholders vote against the acquisition;

    (b) the benefits the acquiring shareholder is expected to bring to the company;

[8] The acquirer's holding or control is aggregated with those of all its associates when determining whether the 20% threshold is going to be exceeded.
[9] If the acquirer already holds or controls more than 50% of the voting rights it may be able to "creep" by 5% under rule 7(e) without needing shareholder approval.

(c) the effect on control of the company. What would the shareholding blocks be after the acquisition? Who might have effective control? and,

(d) the implication for the pricing of possible subsequent control transactions, given the effective control that might flow from the acquisition under consideration.

71. The Panel would prefer not to see advisers refer to transactions as being "fair" or "not fair" to shareholders. See paragraphs 31 and 32 above for the Panel's views on discussions about the "fairness" of transactions.

Rule 18 report – allotments (rule 7(d))

72. A rule 7(d) allotment is one where the allotting company allots shares to the allottee which results in the allottee (together with any of its associates) holding or controlling more than 20% of voting rights in the Code company (or, if the allottee already holds or controls more than 20% of the voting rights, a higher percentage of voting rights).

73. Given that the adviser must have regard to the interests of the persons who may vote on the allotment, the nature of the report will vary depending on whether the allotment is one in which all shareholders participate (such as a pro-rata rights issue underwritten by a major shareholder) or not.

74. If the allotment being made is one where all shareholders have the right to participate then the merits of the allotment could include, among others:

(a) how the allotment price relates to a number of different reference points, including, but not limited to:

(b) the recent market values of the allotting company's shares;

(c) a valuation of the whole company;

(d) discounts observed in other allotments or placements in the market;

(e) the likely value of any rights to acquire shares that shareholders may receive, whether they are tradeable, and the impact on a shareholder's existing holding if the rights are not exercised (and an underwriting shareholder increases its control);

(f) the purpose or purposes to which the proceeds of the allotment are intended to be put;

(g) if there is a major shareholder underwriter of the issue:

(i) the process the Code company followed before deciding to enter into an underwriting agreement with the major shareholder;

(ii) the basis on which the underwriting terms were agreed with the underwriting shareholder and whether they reflect arm's length terms;

(iii) the likelihood of the underwriter being called upon; and

(iv) the ongoing effect on the control and direction of the company if there is a significant shortfall in subscriptions to the issue, with the unsubscribed shares to be taken up by the underwriter;

(h) the effect on control of the company if the non-associated shareholders (i.e., those for whom the report is being written and who will have the opportunity to vote on the allotment) participate, or do not participate, in the offer; and

(i) the consequences for the non-associated shareholders and the Code company if the shareholders vote against the allotment.

75. Again, the Panel expects the allotment to be described and considered in terms more sophisticated than simply "fairness" or "unfairness".

76. If the allotment is one in which the non-associated shareholders will not have the right to participate, but is one where the principal allottee is intended to obtain a significant stake, or increase an existing stake, in the allotting company, the only issue for the non-associated shareholders to decide is whether to vote for or against the proposed allotment. The independent adviser's role is to advise the voting shareholders on the merits of voting for or against the proposed allotment. Those entitled to vote are the Code company's shareholders, excluding the allottee and its associates. As such the voting shareholders are likely to be minority shareholders whose interest in the Code company is being diluted.

77. Factors that the adviser could consider in such a report may include, among others:

(a) the purposes to which the consideration for the allotment (if cash) will be put;

(b) if the allottee is contributing business assets rather than cash, how these will change the existing business of the Code company. Comment on the value of the assets may be appropriate. Are there other benefits of a strategic or marketing nature?

(c) the effect on the control position of non-associated shareholders in the Code company if the allotment proceeds;

(d) a comparison of the issue price with recent market prices for the shares of the issuer and the value of the company, and its likely effect on the future market value of the non-associated shareholders' shareholdings (diluting effect). A full valuation of the Code company may not be necessary. However, the adviser should consider:

(i) whether there is any likelihood of value transfer to the allottee as a result of the proposed allotment;

(ii) the assumptions underlying the issue price for the shares to be allotted; and

(iii) the solvency risk for the Code company if the proposed allotment is not approved by the shareholders; and

(e) the consequences for the company and the non-associated shareholders if the allotment is not approved. Could the company fail? Could the company be foregoing a valuable opportunity to obtain new capital that may not arise again?

Reports for share buybacks

78. Clause 3(g) of Schedule 1 of the Takeovers Code (Class Exemptions) Notice (No 2) 2001 (the "Class Exemptions Notice") relating to buybacks approved by shareholders, provides, as a condition of the exemption, that the notice of meeting containing the proposed resolution to approve the buyback must contain, or be accompanied by:

> a report from an independent adviser, in relation to the buyback, that complies with rule 18 of the Code as if –
>
> (i) references in that rule to an acquisition under rule 7(c) of the Code were references to the buyback by the [Code] company made in accordance with the buyback exemption; and
>
> (ii) the references to a notice of meeting were references to the notice of meeting referred to in this clause.

79. Existing shareholders may increase their control percentage through a buyback undertaken by a Code company in which they do not participate ("the increasing shareholders"), either because the offer is not made to them (selective buy-back) or they opt not to accept the offer.

80. If shareholders not associated with the increasing shareholders approve the buyback for the purposes of the Code, under clause 4 of the Class Exemptions Notice the increasing shareholders may retain their resultant increased control percentages.

81. If the non-associated shareholders do not approve the buyback for the purposes of the Code then the increasing shareholders must, within six months of increasing their control percentage, eliminate the increase to their shareholdings so that their control percentages revert to pre-buyback levels (see clause 5 of the Class Exemptions Notice). The increasing shareholder is prohibited from exercising voting rights from the increased control percentage during the six month period.

82. A buyback may take several forms, including:

    (a) an offer in which all shareholders have the potential to participate and that is achieved through on-market transactions at then-current market prices over a period of time;

    (b) a discrete offer at a fixed price made to all shareholders; or

    (c) a discrete offer at a fixed price made to a selected group of shareholders.

83. It may be helpful for the adviser to distinguish between:

    (a) the buyback itself, which may not require shareholder approval for the purposes of the Companies Act and the Exchange's Listing Rules; and

    (b) the potential for an increase in the control percentage of one or more shareholders if the acquisition (buyback) proceeds, necessitating approval of the buyback by the non-associated shareholders for the purposes of the Code.

84. If the buyback is one for a fixed price over a short period of time, with the offer made to all shareholders, or one or a selected group of shareholders, off-market, the adviser may need to consider, among other matters:

    (a) the merits of the buyback transaction itself from the point of view of the shareholders who will have to consider whether or not to accept the offer; and

    (b) the merits of the buyback transaction as concerns its impact on the control of the company from the point of view of the shareholders who have to decide whether or not to approve the buyback and thus allow the increasing shareholder(s) to increase their control percentage in the Code company.

85. From the perspective of the shareholders as recipients of the offer the issues could include, among others:

    (a) a comparison between the price being offered for each share compared with the value of each share pre-buyback offer. The likely impact on the value of shares after the buyback. Comparison of relevant useful financial ratios for each share remaining in the company after the buyback relative to the ratios before the buyback. For example, where net tangible asset backing per share ("NTA") is a useful measure, comparison of the NTA of the shares remaining in the company after the buyback against the NTA of the shares before the buyback?

    (b) the effect of the buyback on the liquidity of the shares. Whether the buyback provides an opportunity for shareholders to cash-up some or all of their shareholding without impacting the market value of the shares, but possibly at the cost of reduced liquidity after the buyback (when the pool of available shares is likely to be also reduced); and

    (c) the company's capacity to fund the buyback. Is this a way of utilising otherwise surplus cash? Will the company have to borrow to fund the buyback? If so, what impact might this have on debt/equity ratios?

86. From the point of view of the shareholders who have the opportunity to vote to approve or reject the buyback for Code purposes, the issues could include, among others:

    (a) whether this is a means by which the increasing shareholder(s) can obtain an increased control percentage without having to pay a premium for the level of control to be achieved; and

    (b) the likely outcome if the shareholders vote against the proposal. For example, will the buyback still go ahead, but without the increasing shareholders being able to retain and vote their increased control percentages? What are the prospects of the increasing shareholders making a Code offer to all shareholders?

87. If the buyback is one where shareholder consent is not required under the Companies Act or the Listing Rules, and where acquisitions can take place at market prices at any time over a future period, the issues may be slightly different. The buyback transactions will occur at prevailing market prices when the directors consider it is in the best interests of the shareholders and the company for the company to buy its own shares. There is thus

no fixed reference point against which to assess value. In this case comments could cover matters, among others, such as:

(a) a comparison between current market prices and the assessed value or NTA value, if relevant. What would be the effects on the assessed value or the NTA of remaining shares if the buyback proceeds at current market value?

(b) the benefits for shareholders if the buyback proceeds;

(c) the likelihood of the buyback proceeding anyway if the shareholders vote against the buyback for the purposes of the Code;[10]

(d) the prospects of all shareholders being able to participate in the buyback. Not all shareholders are likely to want to take the opportunity to sell into the buyback;

(e) the implications for control of the company if the buyback is approved; and

(f) the options available to the increasing shareholders if the shareholders vote against the buyback. Is an increasing shareholder able to "creep" under rule 7(e)? Might an increasing shareholder make a full or partial takeover offer for the company?

88. As with other Code transactions, the Panel prefers that the buyback offer not be described in terms of its "fairness" or "unfairness" to the voting shareholders.

89. In all buybacks, the fundamental reason for the meeting under clause 4 of the class exemptions is for the non-associated shareholders to effectively approve (by their approval of the buyback) the increasing shareholders obtaining an increased level of control of the company.

Reports for Compulsory Acquisitions

90. In broad terms, rule 57 relates to cases of compulsory acquisition where a person (whether alone or acting jointly or in concert with one or more other persons) has become a dominant owner (i.e., has become the holder or controller of 90% or more of the voting rights in a Code company by means other than a takeover offer (for example, on-market acquisitions). In such cases, the consideration specified in the acquisition notice under rule 55 of the Code, for the purposes of a compulsory acquisition of the outstanding securities in the Code company must be a cash sum certified as fair and reasonable by an independent adviser.

91. For the purposes of rule 57, the fair and reasonable value of an equity security must be calculated by:

(a) first assessing the value of all the equity securities in the class of equity securities of which the equity security forms part; and

(b) then allocating that value pro rata among all the securities of that class.

[10] If this occurs the increasing shareholders would have to reduce their increased control percentage back to pre-buyback levels within six months, and could not exercise those increased voting rights in the six-month period.

92. The consideration specified in the acquisition notice is not necessarily the price payable on compulsory acquisition. The price may be subject to adjustment if, within 14 days of sending the acquisition notice, the dominant owner receives written objections to the specified consideration from outstanding security holders who hold the lesser of:

    (a) 2% or more of a class of equity securities; or

    (b) 10% or more of the outstanding securities of a class.

93. In that event, the dominant owner must immediately refer the amount of the consideration to an expert determination. The expert is an independent person appointed by the Panel (rule 58(1)) and the costs must be paid by the dominant owner (rule 58(3)). The expert must determine the consideration and it must be a cash sum equal to the fair and reasonable value of the securities of the relevant class (rule 57(3)).

94. The rule 57(1) certificate should include a valuation of the Code company. This is important because outstanding security holders can object to the acquisition consideration. Accordingly, in order to exercise their objection rights in a considered manner, the outstanding security holders should have access to the financial analysis undertaken by the independent adviser.

95. The other matters to be considered by an independent adviser who is preparing a rule 57(1) certificate are likely to be quite limited. An issue that may arise could be the value paid by the dominant owner in recent acquisitions of securities in the Code company. The adviser may need to comment on such transactions in light of the value of the cash sum for the acquisition consideration.

96. The rule 57(1) certificate is not required by the Code to accompany the acquisition notice that is sent to the outstanding security holders. However, the dominant owner must send a copy of the certificate free of charge on request to any person (i.e., outstanding security holders) within one day of the request (rule 57(5)). A similar requirement applies if the consideration is referred to expert determination (rule 57(6)).

97. However, the Panel considers that it is best practice for dominant owners to send the rule 57 certificate together with the acquisition notice to the outstanding security holders. This may assist the outstanding security holders in deciding whether to make an objection to the acquisition consideration.

Appendix A

The Panel's Policy on the Approval of Independent Advisers

General Information

1. Under the Takeovers Code, reports from independent advisers are required in various circumstances.

   (a) Rules 15 and 16 require such a report where a person seeks to acquire or have allotted to it voting securities in a Code company (or in some circumstances in another body corporate) with shareholder approval;

   (b) Rule 21 requires the directors of a target company to obtain a report from an independent adviser on the merits of an offer;

   (c) Rule 22 requires the offeror to obtain a report from an independent adviser where an offer is made for different classes of securities;

   (d) Rule 57(1) requires an independent adviser to certify in some circumstances that the cash sum proposed as consideration for a compulsory acquisition of equity securities under the Code is fair and reasonable; and

   (e) Some exemptions granted by the Panel include a condition that a report from an independent adviser be prepared in relation to the transaction the subject of the exemptions.

2. An "independent adviser" means "an adviser whom the Panel considers is independent and who is approved by the Panel for the purposes of" the Takeovers Code.

3. Independent advisers' reports play an important role in the scheme of the Code. The Panel takes its responsibilities for approving the appointment of independent advisers very seriously. The paragraphs below set out the Panel's criteria for approval as an adviser.

The Panel's criteria for approval

4. The current policy of the Panel is to consider each application for approval on a case by case basis so that the Panel can be satisfied, on each occasion, that:

   (a) the adviser is appropriately qualified and experienced; and

   (b) independent.

5. In considering an application, the Panel may also take into account any other factors that it considers relevant for the purposes of the Code in relation to the appointment for which the adviser seeks approval.

6. If the adviser has previously provided a report for the Code company in question, the Panel will also need to be satisfied that:

(a) the adviser would not be constrained by the methodology or views expressed in its earlier report; and

(b) the degree of familiarity (if any) between personnel at the adviser firm and personnel at the Code company would not compromise the adviser's independence.

7. The Panel will approve the appointment of an independent adviser in advance of a proposed transaction on the basis that:

(a) the identities of all the parties to the proposed transaction are ascertainable and the Panel is satisfied that the proposed adviser does not have any conflicts of interest with those parties which could compromise its independence; and

(b) there is a reasonable likelihood that the proposed transaction will proceed.

8. If the proposed transaction is delayed for a significant period of time from the date that the Panel approved the appointment of the adviser, the Panel will need to be satisfied that the adviser is still independent.

9. The Panel will keep this policy under review and is not bound by prior decisions.

Conflicts of interest

10. Every prior or existing relationship between the adviser and any relevant entity must be disclosed to the Panel but it will not automatically disqualify the adviser from being approved. The Panel will consider the nature and extent of any prior or existing relationships before an approval can be given.

11. The following types of relationship may lead the Panel to conclude that the proposed adviser is **not** independent:

(a) if the proposed adviser has been involved in giving strategic advice on the relevant transaction to any party;

(b) if the proposed adviser is likely to financially benefit from the success or failure of the relevant transaction;

(c) if the proposed adviser has an ongoing corporate advisory role for any party to the relevant transaction; and

(d) if the proposed adviser has an interest in any party to the relevant transaction.

12. A proposed adviser that has some form of relationship (other than those listed above) with a party to the transaction will not automatically be precluded from being approved. The Panel will look at the facts and circumstances of each case.

Successive transactions

13. In some cases, a Code company that is subject to successive Code-regulated transactions (for example, follow-on takeover offers) may wish to appoint the same adviser from an earlier transaction to prepare the new report.

14. The Panel will consider whether the shareholders are likely to benefit from having an independent adviser's report prepared by a different advisory firm from that which prepared the earlier report(s), and may consider the following factors:

    (a) the proximity of the preparation, and nature, of the earlier report(s);

    (b) whether the currently required report is likely to be the last independent adviser's report to be provided to shareholders before compulsory acquisition is initiated;

    (c) whether the business, circumstances or prospects of the Code company have changed since the earlier report(s); and

    (d) the relationship between the value given in the adviser's earlier report(s) and the offer price(s) under the successive offer(s).

Use of sub-contractors

15. In some cases, the firm putting itself forward for approval as an independent adviser for a particular Code transaction will not have the necessary expertise to deal with all aspects of the assignment. In these cases, the firm may engage the specialist services of a subcontractor to assist with the report.

16. The Panel expects to consider the appointment of the proposed subcontractor at the same time as it considers the application by the primary adviser. The Panel must be satisfied that:

    (a) The subcontractor has the necessary expertise and independence to undertake the assignment;

    (b) The subcontractor has been chosen by the primary adviser and not, for example, by the target company or offeror; and

    (c) The work of the subcontractor will be managed by the primary adviser.

Advice in advance of making an application

17. If a proposed adviser has any reservations about making an application to the Panel due to a relationship with a party to the relevant transaction or some other concern, the Panel encourages advisers to contact the Panel executive for guidance. The Panel executive welcomes any queries and can be contacted at the numbers listed on the website or on (04) 815 8420.

Appendix B

Information required in an application for approval as independent adviser

1. Applications should be submitted to the Panel (see the contact details at the end of this Appendix) by the proposed independent adviser and must include the information set out below. This will ensure that all necessary information is provided and delays caused by an incomplete application are avoided.

2. Each application should include:

   (a) Transaction background information*:*

      (i) a brief outline of the Code transaction or series of transactions to which the appointment relates;

      (ii) the relevant rule in the Code for the report (i.e., 18, 21, 22, 57) or the relevant exemption;

      (iii) the names of the persons instructing the applicant and any other key parties in the relevant transaction or series of transactions; and

      (iv) the directors and substantial security holders of each of those parties.

   (b) Applicant's details:

      (i) the applicant's legal name, address, place of business and contact details; and

      (ii) details of the directors and shareholders of the applicant (if applicable).

   (c) Qualifications and experience:

      (i) a statement of the qualifications and expertise of the applicant, in the form the applicant expects it to appear in its report;

      (ii) names and curricula vitae of the individuals who will be involved in preparing the report;

      (iii) evidence of previous relevant experience demonstrating the applicant's suitability for approval;

      (iv) *if the applicant is a sole practitioner,* the Panel may require confirmation from the applicant that, if the applicant is approved, someone of appropriate standing would undertake a peer review of the report. The details of the peer reviewer should also be provided; and

      (v) *if the Panel is unfamiliar with the applicant's work,* the applicant should submit examples of previous work undertaken, as evidence of the applicant's expertise.

(d) Independence:

(i) A statement that the applicant has no conflict of interest that could affect the applicant's ability to provide an unbiased report. It is a requirement of the Takeovers Code that the independent adviser include this statement in their report. Accordingly, *the Panel will not accept any qualification to this statement*; and

(ii) the applicant must disclose:

A. all past and present relationships (whether professional or otherwise) between the applicant and the persons instructing the applicant or any other party to the transaction or series of transactions (including the directors and the substantial shareholders (i.e., those shareholders with a relevant interest of 5% or more of the securities) of any such parties). This disclosure should give the nature, extent and duration of the relationship, including the fees earned, the timeframe of the assignments and whether there has been any past, or is any present, involvement with any of the parties as auditor. If there are no such relationships, a statement to this effect;

B. any advisory activities which the applicant is, or will be, undertaking in relation to this transaction, including details of the basis of remuneration for such activity. Such activities might include, for example, the provision of an independent appraisal report under the Listing Rules. If there are no such activities, a statement to that effect;

C. any direct or indirect pecuniary or other interest, including any success or contingency fee or remuneration, other than the applicant's fee for providing the report. If there are no such interests, a statement to that effect;

D. any prior involvement in the transaction (particularly in the formulation of it). If there was no prior involvement in the transaction, a statement to that effect;

E. if the applicant is preparing an appraisal report under the NZX Listing Rules, this should be stated;

F. the date on which the applicant was first approached by the person instructing the applicant (the “appointor”) about the work to which the application relates;

G. to the best of the applicant’s knowledge, whether the appointor utilised a competitive process in choosing the applicant for the work to which the application relates;

H. whether the applicant and the appointor discussed the valuation methodology to be used in the proposed engagement; and

I. whether the applicant and the appointor discussed the price and/or any parameters of the valuation.

Other information

3. The application must also contain the following statements:

   (a) a statement certifying that the applicant's professional liability insurance cover is adequate in relation to the size of the transaction;

   (b) a statement that the applicant has adequate resources to complete the assignment within the required timeframe;

   (c) a statement as to the timeframe within which the applicant would like the Panel to respond; and

   (d) if appropriate, the names of any Panel members the applicant considers might be conflicted from making a decision in respect of the matter and why the applicant considers this to be the case.

Information required by person instructing the applicant (the "appointor")

4. The application must also contain the following:

   (a) A request in writing from the appointor that the applicant be approved. The Panel executive will not process the application until it has received this request; and

   (b) a statement in writing of the process undertaken by the appointor to select the applicant. The statement must include, but is not limited to, the following information:

      (i) the date on which the appointor approached the applicant in respect of the proposed engagement;

      (ii) whether the appointor utilised a competitive process to choose the applicant;

      (iii) how many firms were considered by the appointor for the proposed engagement;

      (iv) the factors that were taken into account by the appointor in determining whether to appoint the applicant;

      (v) whether the appointor and the applicant discussed the valuation methodology to be used in the proposed engagement; and

      (vi) whether the applicant and the appointor discussed the price and/or any parameters of the valuation.

Use of subcontractors

5. If the adviser wishes to engage the services of a subcontractor to prepare some aspect of the report (e.g., an asset valuation), the application must also contain:

   (a) the proposed subcontractor's background information, qualifications, experience, and independence (see above for the information required); and

(b) a statement from the principal adviser that:

(i) the subcontractor has the necessary expertise and independence to undertake the assignment;

(ii) the subcontractor has been chosen by the primary adviser and not, for example, by the target company or offeror;

(iii) the work of the subcontractor will be managed by the primary adviser; and

(iv) a statement from the proposed sub-contractor that it has no conflict of interest that could affects its ability to provide an unbiased report.

6. Applications may be sent to the Panel at the contact details listed at the end of this Appendix.

7. The application fee for an approval application is $112.50 (including GST), as prescribed under the Takeovers (Fees) Regulations 2001. These regulations also prescribe the hourly rates chargeable for time spent on the application by Members of the Panel and by professional staff. Applicants will be sent an account at the conclusion of the Panel's work or on a monthly basis.

8. The Panel is aware that applications often need to be dealt with expeditiously and will endeavour to meet the applicant's timeframe. Processing time depends on the nature and quality of the application and the resources available within the Panel at the time the application is sent. The Panel's decision will be notified to the applicant as soon as possible after it is made.

9. The Panel endeavours to make a decision on an application for approval to act as an independent adviser within three working days of the date on which the Panel receives all the information required for an application. The Panel executive has a delegated authority to approve independent adviser applications in some cases. This will usually reduce the costs and processing times for applications.

10. The Panel reserves the right to amend this policy.

Appendix C

Statement of Independence

1. The Panel requires independent advisers to display a "Statement of Independence" on the front cover of their report.

2. The statement is this:

STATEMENT OF INDEPENDENCE

[Name of adviser] confirms that it:

- has no conflict of interest that could affect its ability to provide an unbiased report; and

- has no direct or indirect pecuniary or other interest in the proposed transaction considered in the report, including any success or contingency fee or remuneration, other than to receive the cash fee for providing this report.

[*For a Code-regulated transaction*]

[Name of adviser] has satisfied the Takeovers Panel, on the basis of the material provided to the Panel, that it is independent under the Takeovers Code for the purposes of preparing this report.

[*For a Scheme of arrangement*]

[Name of adviser] has satisfied the Takeovers Panel, on the basis of the material provided to the Panel, that it is independent under the Panel's Guidance Note on Independent Advisers and the Takeovers Code for the purposes of preparing this report.