# CASE NOTE*

# A MODEST JUDGMENT ON WHAT SHOULD AND SHOULD NOT BE IN TAKEOVER DOCUMENTS? OR A NEW DISCLOSURE STANDARD FOR SCRIP TAKEOVERS AND NEW ISSUE PROSPECTUSES?

*PANCONTINENTIAL MINING LIMITED v GOLDFIELDS LIMITED*

A financial journalist, writing soon after the $440 million takeover battle for Pancontinental Mining Limited had emerged from the Federal Court, noted that Justice Tamberlin had probably set out to produce "a modest judgment on what should or should not be in takeover bid documents".[1] In a sense, of course, this is true of any contested takeover in which one side seeks to litigate on the basis of alleged defects in the opposing side's takeover documents. Yet, as the journalist in question recognised, *Pancontinental Mining Limited v Goldfields Limited*[2] repays a closer reading.

The judgment, which is notable for its strongly commercial approach to takeover litigation, is likely to impact upon future scrip takeover bids as well as new issue prospectuses. It is also interesting for its general approach to disclosure of complex information to shareholders who are asked to make important financial decisions on the basis of such information.

---

* David Nathanson, BCom LLB (UNSW), Solicitor, Freehill Hollingdale & Page.

1 I Ries, "Renison judgment sets new standard" *Australian Financial Review*, 4 April 1995.

2 (1995) 13 ACLC 577.

# I. THE FACTS

## A. The Offer

On 1 March 1995, Goldfields Limited ("Goldfields") served a Part A Statement on Pancontinental Mining Limited ("Pancon") relating to takeover offers for all of the issued shares in Pancon.

Goldfields is a subsidiary of Renison Goldfields Consolidated Limited ("RGC"), the holding company of a diversified mining and mineral exploration group with operations in Australia, Papua New Guinea and other countries.

The consideration offered by Goldfields was one Goldfields share plus $2.10 cash for every three Pancon shares. At the time, Goldfields was not listed on the Australian Stock Exchange.

Goldfields' Part A Statement was a substantial and complex document extending to well over 250 pages. It was claimed to be one of the most complicated (if not the most complicated) Part A Statement yet delivered in an Australian takeover.[3] This was largely because of the planned post-acquisition restructure of the offeror, and the associated financing complexities that went along with that restructure.

## B. Rationale and Structure of the Bid

Goldfields suggested in its Part A Statement that the Australian sharemarket frequently attributes a premium to major Australian gold producers in comparison to major diversified mining companies (evidenced by average multiples of price to prospective cash flows).

In the event that Goldfields' takeover bid resulted in it acquiring full control of Pancon, Goldfields intended to cause Pancon to sell all of its non-gold assets to RGC. RGC would, at a later point, sell some of its gold assets into Goldfields, creating an exclusively-gold producing company. The purpose of the restructure was therefore to enable Goldfields to attract a potential market premium and to present a more attractive investment opportunity to shareholders.

## C. Financing the Offer

RGC was to finance the takeover by an issue of convertible unsecured notes at a subscription price of $3.30 per note. RGC would lend the funds received from the issue to Goldfields interest free. Until they converted into Goldfields shares, the convertible notes were in the nature of debt obligations of RGC. They would convert if the takeover became unconditional and Goldfields attained more than 50 per cent of Pancon's shares.

If the takeover did not succeed, and the convertible notes did not convert, RGC would redeem the notes at a premium.

---

3 *Ibid* at 582.

### D. Pancon's Attack

Pancon applied for a declaration that Goldfields' Part A Statement did not comply with s 750 of the *Corporations Law*, together with an order that Goldfields be restrained from making any offer as referred to in the Part A Statement.

Pancon's challenge to the Part A Statement was based on a wide range of grounds relating to non-compliance with s 750, as well as claims of misleading and deceptive conduct under ss 995(2) of the Law.

## II. THE LEGISLATIVE FRAMEWORK

### A. Part A Statements - s 750

A Part A Statement is a disclosure statement prepared for the information of shareholders and directors of a target company. The Part A Statement is intended to satisfy the objectives of the legislation that shareholders and directors know the identity of a person who proposes to acquire a substantial interest in the company and are supplied with sufficient information to enable them to assess the merits of such a proposal.[4]

A document is only a "Part A Statement" if it complies with Part A in s 750. If it fails to do so, the takeover offers will not constitute a takeover scheme and, accordingly, will be illegal for breaching the basic prohibition contained in s 615.

Section 750 is very specific about the information required to be contained in a Part A Statement. The clauses of s 750 relevant to the case were as follows:

> 17. The statement shall set out any other information material to the making of a decision by an offeree whether or not to accept an offer, being information that is known to the offeror and has not previously been disclosed to the holders of shares in the target company.
>
> 18. If the statement...is included in a class of Part A statements in relation to which regulations are in force for the purposes of this paragraph...the statement shall set out the prescribed matters...

By regulations 6.12.01 and 6.12.02, where the consideration under a takeover scheme includes shares, the Part A Statement must contain the information that would be required to be included if the Statement was a prospectus.

Under s 1022(1) of the Law a prospectus must (in addition to the information specifically required by s 1021) contain:

> ...all such information as investors and their professional advisers would reasonably require, and reasonably expect to find in the prospectus, for the purpose of making an informed assessment of the assets and liabilities, financial position, profits and losses and prospects of the corporation...
>
> (a) the assets and liabilities, financial position, profits and losses, and prospects of the corporation; and...

4 These comprise two of the so-called 'Eggleston principles' now enshrined in s 731 of the *Corporations Law*.

### B. Misleading and Deceptive Conduct - s 995(2)

Section 995(2) provides that a person shall not, in connection with the allotment or issue of securities, or any prospectus issued or notice published in relation to securities, or the making of takeover offers, "engage in conduct that is misleading or deceptive or is likely to mislead or deceive".

## III. THE DECISION

While most of the grounds of attack raised by Pancon were dismissed, Tamberlin J held that in three significant areas the Part A Statement was deficient.

### A. Deficiencies in the Part A Statement

*(i) Forecast of Earnings Information*

Pancon argued that the Part A Statement should have included either a discounted cashflow valuation ("DCF") of Goldfields' assets or a forecast of Goldfields post-acquisition earnings and dividends. Pancon claimed that such information was necessary to enable shareholders to make a proper decision whether to accept the offer, and to make an assessment of the prospects of the new entity. This was all the more necessary, it was argued, because the offeror had no 'track record' in the market or any earnings history. Because Goldfields was a new company, the Goldfields scrip being offered to Pancon shareholders could not easily be valued by shareholders.

Goldfields' Part A Statement contained neither a DCF analysis nor an earnings and dividend forecast.

Pancon led uncontested evidence of eight recent prospectuses issued over the past two years by new mining companies. While only one contained a DCF analysis, in all eight there were earnings forecasts for either the current year (four companies) or for two years (four companies).

The thrust of Goldfields' argument, by contrast, was directed to suggesting that an astute investment adviser would be able to make an informed judgment as to the post-acquisition prospects of Goldfields' by drawing together information contained in various parts of the prospectus.

Tamberlin J held that a DCF analysis was not required. This was because there was no evidence that there had been a consistent practice of providing a DCF analysis in prospectuses issued by mining companies. Indeed, the evidence was to the contrary.[5]

> However, his Honour was of the view that Pancon and its offeree shareholders were entitled under the Corporations Law to the benefit of an earnings forecast over at least a two year period.

---

5 The absence of DCF analyses in mining prospectuses may be explained by the fact that an effective DCF analysis requires a forecast of earnings over at least ten years, with a large number of critical assumptions involving matters inherently difficult to predict, such as gold prices, exchange rates and production costs: see Note 2 *supra* at 583.

> In my view, the inclusion in each of these prospectuses of earnings forecasts affords clear and substantial support for the view that earnings and dividend forecasts provide material information which investors and their advisers would *reasonably require* and *reasonably expect to find* in such documents for the making of an informed assessment of the prospects of the corporation.[6]

In response to Goldfields' argument, Tamberlin J asked why, if the necessary information could be found in the Statement, had Goldfields not drawn it together and clearly set out the result in an appropriate and prominent part of the Statement?

> An offeree, when faced with a complex and length prospectus...should not have to forage through the whole prospectus, seeking out fragments of information in order to piece together the assumptions and construct a forecast of earnings, from a number of disparate and indirect scattered references in a 250 page document. If the information is there, the offeror should perform the exercise and not leave it to the offeree to make assumptions... The offeree is entitled to have the forecast clearly set out, in a lucid and direct form, in a prominent part of the Statement, so that attention can be focused on the critical matter of earning potential.[7]

As Tamberlin J noted, not every offeree will have a sophisticated investment consultant at hand when reviewing the Statement to perform arcane valuation exercises.[8]

*(ii) Papua New Guinea - Risks*

Pancon claimed that, because it had no operations in Papua New Guinea, the Part A Statement should have spelled out in detail the political, legal and other risks involved in gold mining in that country. This was because, by accepting Goldfields' offer, Pancon's shareholders would become shareholders in a gold mining company with operations in Papua New Guinea.

Pancon argued that mining in Papua New Guinea involves greater risks than mining in Australia. It referred to risks relating to the Papua New Guinea economy, possible challenges to the Papua New Guinea Mining Act, the application of legislation relating to fairness of transactions, risks arising from civil unrest, risks of expropriation, changes in taxation, claims by owners of the land for its return and foreign exchange.

The only specific reference to investment risks in the Part A Statement was a one line statement that "offshore exploration and mining activities may be subject to political risk". There was also some general information about the risks of mining in Papua New Guinea in the report of the independent geologist and engineer.

Tamberlin J found that the disclosure in this respect was "clearly inadequate". What was required, in his view, was

> ...a comprehensive Statement raising and dealing with the political and other risks of mining and operating in Papua New Guinea making particular specific reference to the problems experienced by RGC/Goldfields. There should be some discussion of the significance attributed by Goldfields to those risks.[9]

6 Note 2 *supra* at 583.
7 *Ibid* at 585.
8 *Ibid.*
9 *Ibid* at 593.

*(iii) The $3.30 Valuation of Goldfields Shares*

As noted previously, the consideration offered by Goldfields was one Goldfields share plus $2.10 cash for every three Pancon shares. Because Goldfields was a new entity with no market price, Pancon shareholders were unable to calculate the value of the consideration themselves.

In its Part A Statement, Goldfields had stated that "[b]y calculating the value of the Goldfields Shares at the [c]onverting...underwritten price of $3.30, the consideration offered for each Pancontinental Share would be $1.80, which includes $0.70 cash."

Pancon claimed that the converting underwritten price was not a reliable indicator of the value of such a share. It also claimed that it was misleading to represent that a Goldfields share when issued would have a value of $3.30.

Goldfields argued that the underwritten price of the converting security provided guidance as to the likely value of a Goldfields share because the underwritten price and its underwriting terms provided an assessment of the probable minimum value which the underwriter had placed on the shares. The expert witness called by Pancon acknowledged in cross-examination that this was indeed *one* way of calculating the likely prospective price of the Goldfields shares when floated.

Tamberlin J held that, since the Part A Statement made it quite clear that the assumed post-acquisition price of the Goldfields shares was based on the convertible note conversion price, the Statement could not be classified as misleading. However, he continued:

> [T]here is a significant omission in the Statement as to how the figure is arrived at. Since the figure is of central importance to the takeover scheme, I consider that the offeree shareholders in Pancontinental would regard as material the data and methodology by which this figure was arrived at...[10]
>
> The data and reasoning...should be properly set out and made available in the Part A Statement so that it can be considered by the offerees and the board of Pancontinental. Otherwise the offeree is required to accept the opinion of the underwriter without any information as to how or why that price was chosen.[11]

The makeup of the $3.30 was thus clearly of material importance for Pancon shareholders when considering whether to accept or reject the offer.

Accordingly, Tamberlin J held that while the $3.30 figure was not misleading within s 995(2), the omission of any justification as to its basis was a material omission in contravention of the requirements of s 750.

## B. Conclusions and Orders

Despite the fact that the Part A Statement contained important omissions of material information in contravention of clauses 17 and 18 of s 750, Tamberlin J did not consider that there had been any intention on the part of Goldfields or RGC to contravene the Law:

> [A]lthough the omissions go to matters of substance and importance, I do not consider that it is appropriate that the Part A Statement should be invalid. What is called for in

10 *Ibid* at 594.

11 *Ibid* at 595.

> the interests of offeree shareholders...is the provision of proper additional information on the matters omitted from the Statement to enable the shareholders to make their decision whether to accept the offer on a fully informed basis.[12]

Accordingly, Tamberlin J made an order under s 739 of the Law to the effect that, if Goldfields wished to proceed with its takeover, it should supply Pancon shareholders with supplementary information concerning the omitted matters, and he restrained distribution of the Part A Statement and offers unless accompanied by the specified information. On the condition that the information was provided, his Honour made an order under s 743 of the Law validating the Statement.

## IV. COMMENT

The case is significant in a number of respects.

By ordering Goldfields to provide specific supplementary information to shareholders if it wished to proceed with its takeover, the Court in effect settled the contents of the Part A Statement for the parties. In contrast to the alternative approach, in which a Court merely pronounces upon the validity or otherwise of takeover documents, the more interventionist approach exhibited by Tamberlin J is consistent with a statutory scheme "designed to facilitate the making and consideration of takeover offers and the making of informed decisions in a commercial environment which is often volatile and requires dispatch and efficiency".[13] The demands of the commercial environment, and the importance of early dispatch and efficiency, were emphasised by the events which followed the ruling. Having handed down his decision on a Friday afternoon, Tamberlin J found himself on the following Wednesday considering (and approving) a 35 page supplementary information booklet prepared by Goldfields to meet the shortcomings of its earlier document.

The decision is also interesting for its approach to the interaction between s 995(2) and s 750. It is clear that omission or silence may constitute conduct which is likely to mislead or deceive.[14] Tamberlin J regarded Goldfields' failure to explain the methodology behind the $3.30 valuation of its shares as a "significant omission" in relation to a matter of "central importance" to the takeover scheme. This failure, along with the omission of an earnings forecast and information regarding the risk factors of investing in Papua New Guinea, meant that the Part A Statement contravened clauses 17 and 18 of s 750. The information provided in the supplementary information booklet to remedy these defects ran to 35 pages. Yet in spite of this, his Honour held that the Part A Statement was not misleading or deceptive within s 995(2). While perhaps open to technical argument, it is submitted that the result is a commercially practical one.

---

12 *Ibid* at 599.

13 *Ibid* at 582. Tamberlin J followed the approach taken in *Target Petroleum NL v Petroz NL* (1987) 16 FCR 1 at 13.

14 This has been established in a number of cases on s 52 of the Trade Practices Act (which provides a useful guide to the interpretation of section 995(2)). See, for example, *Demagogue Pty Ltd v Ramensky* (1992) 39 FCR 31.

Shareholders had not received the Part A Statement (and could not have been misled) and the offeror was quickly able to remedy the omission and dispatch its documents.

Perhaps the most interesting aspect of the judgment was Justice Tamberlin's ruling that Pancon shareholders were entitled to the benefit of a two year earnings forecast. Although his Honour held that an earnings forecast was required on the facts before him, he was careful to note that information as to earning potential was not necessarily essential in every case as a matter of law:

> What is material in a takeover scheme is a matter for judgment and assessment in the light of all the evidence, facts and circumstances in each particular takeover context and this will necessarily differ from case to case. Differing circumstances can include, for example, matters such as relevant public information available, material already disclosed by the offeror, the activities of the target company and the location of those activities; and the probable knowledge or awareness of the shareholders in the target company as to particular subject matters.[15]

Clearly, an earnings forecast will not be required in all cases. When the company making a takeover bid is a listed company which complies with the continuous disclosure obligations contained in the *Corporations Law* and Listing Rules, shareholders on the receiving end of a scrip bid will have no need of a two year earnings forecast to assess the value of what is being offered to them. Indeed, if such companies have been "disclosing entities"[16] for more than 12 months, from September 1995 they will be subject to the less onerous prospectus requirements contained in s 1022AA(2).[17] Accordingly, if such a company launches a scrip takeover bid, the information required to be included in its Part A Statement will extend only to the information required by that subsection.

The effect of the decision should therefore be limited to scrip bids in which part of the takeover consideration offered to target shareholders consists of shares in a new entity, as occurred on the facts of this case. Importantly however, should a Part A Statement in these circumstances be challenged again, the parties will now be expected to lead evidence as to what information investors and their advisers would "reasonably require and reasonably expect to find" in the document for the purpose of assessing the assets and liabilities, financial position, profits and losses and prospects of the company. Precisely what will be required will be critically influenced by the nature of this evidence, and may differ from company to company and industry to industry.

This aspect of the decision will affect not only scrip takeover bids but also new issue prospectuses, which have received little judicial consideration since the *Corporations Law* prospectus provisions replaced the old co-operative scheme legislation. Interestingly, it had been assumed by some that the reference in

---

15 Note 2 *supra* at 588.

16 See the definition in s 111AC(1).

17 Under s 1022AA(2)(b) the prospectus must contain "all such information as investors and their professional advisers would reasonably require, and reasonably expect to find in the prospectus, for the purpose of making an informed assessment of:

(i) the effect of the offer...on the disclosing entity; and

(ii) the rights attaching to the securities..."

s 1022(1) to information reasonably required to assess the "prospects" of the corporation did not necessarily require a specific profit forecast - it was assumed that the company's prospects could be dealt with without any tables or figures.[18] Such an argument is probably no longer tenable. The approach taken by Tamberlin J indicates that courts are now more likely to hold that investors and their advisers will reasonably expect to find earnings forecasts in a new issue prospectus to enable them to assess the prospects of a new company offering shares to the public. Again, however, the nature of the evidence will be critical to a court's decision about what level of earnings disclosure is required, companies will be expected to lead evidence concerning the extent of earnings forecasts contained in recently issued prospectuses of comparable companies.[19]

Finally, the ruling is significant for strengthening the recent judicial trend towards approaching takeover documents and prospectuses from the perspective of the average investor. Twice in the course of his judgment, Tamberlin J stated that it was not sufficient for Goldfields to argue that the Part A Statement contained all the information that an investor required and that an astute investor could draw it together from the scattered references throughout the document.

Citing *Fraser v NRMA Holdings Ltd*,[20] his Honour stated:

> The objective is to present a document which can be understood by members of the public and which does not confuse. This includes a considerable degree of selectivity designed to confine the information to that which is really useful.[21]

As first expressed in the American case of *TSC Industries Inc v Northway Inc*, it will no longer be sufficient "simply to bury the shareholders in an avalanche of trivial information".[22]

At a time when the fear of litigation is causing takeover offerors to swamp investors with ever more weighty and complex takeover documentation, Justice Tamberlin's injunction to Goldfields to set out important information "in a lucid and direct form, in a prominent part of the Statement"[23] is to be welcomed.

---

18 See HAJ Ford, RP Austin, *Principles of Corporations Law*, Butterworths (7th ed, 1995) p 826.

19 Whether offering shares as part of a scrip takeover or a new issue, companies (and their directors and advisers) who provide earnings forecasts need to be mindful of s 765 of the *Corporations Law*, which provides that if a person makes a representation with respect to a future matter, that person has the burden of proving that there are reasonable grounds for making the representation, or else it is taken to be misleading.

20 (1995) 15 ACSR 590 at 603.

21 Note 2 *supra* at 585.

22 (1976) 426 US 438 at 448.

23 Note 2 *supra* at 585.