REQUISITIONERS BEWARE

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Australia Capital Markets Alert

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- Recent Takeovers Panel declaration confirms that individual shareholders will almost certainty be "associates" for the purposes of a joint requisition.
- Non-disclosure of any actual (or subsequently determined) association will also almost certainty lead to a declaration of "unacceptable circumstances".
- Caution is advisable when utilising the meeting requisition provisions in Chapter 2G of the Corporations Act by shareholders with a combined voting power of 20% or more.

BACKGROUND

In April 2019, three individual shareholders (together, the Requisitioning Shareholders) who collectively held more than 5% of the voting shares in ASX-listed *Aguia Resources Limited* (Company) jointly signed and delivered a requisition to the Company's (now former) board of directors requiring those directors to call and hold a shareholders' meeting in accordance with section 249D[1] of the *Corporations Act 2001* (Cth) (Corporations Act) (Requisition).

The Requisition contained resolutions seeking the removal of a number of the Company's directors and resolutions in relation to the appointment of other directors in which the Requisitioning Shareholders had more confidence. The Requisition was initiated after discussions involving one of the individual Requisitioning Shareholders and the Company's directors broke down.

TAKEOVERS PANEL

Following receipt of the Requisition, the Company's (now former) directors applied to the Australian Government Takeovers Panel (Takeovers Panel) seeking, amongst other things, a declaration that the Requisition constituted "unacceptable circumstances"[2] . In its application, the Company's directors argued that such a declaration was appropriate, in part, because the Requisitioning Shareholders had not disclosed their alleged association[3] (and therefore, their alleged combined "voting power"[4] in the Company[5]) in contravention of the substantial holder notice provisions of the Corporations Act.

In response to the application to the Takeovers Panel, the Requisitioning Shareholders submitted that they were not associates (ie amongst themselves or with any other person) because:

- rather than "acting in concert" in relation to the affairs of the Company and the Requisition, the individual members of the Requisitioning Shareholders had simply "banded together" so that they could collectively satisfy the 5% shareholding threshold required by section 249D, and

- there was no "relevant agreement", commitment, promise or undertaking (whether formal or informal) between any of the Requisitioning Shareholders (ie amongst themselves) or between any of them (ie individually) with any other person in relation to the Requisition or the composition of the Company's board of directors.

THE DECLARATION

In *Aguia Resources Limited* (as to which, see TP19/035) (Aguia Resources) the Takeovers Panel found that the joint signing of the Requisition by the Requisitioning Shareholders coupled with evidence that indicated an alignment of the Requisitioning Shareholders' interests and intentions[6] with regards to the future direction of the Company were sufficient bases upon which the allegation of association could be sustained[7].

In addition, and even though the Requisitioning Shareholders' combined voting power in the Company was below 20%, the Takeovers Panel found that the "non-disclosure" of the Requisitioning Shareholders' subsequently determined "association" contravened the substantial holder notice provisions of the Corporations Act and therefore constituted "unacceptable circumstances" in relation to the affairs of the Company.

The Takeovers Panel said that the declaration of unacceptable circumstances was appropriate because the Requisitioning Shareholders' contravention of section 671B had deprived the Company's other shareholders of meaningful information in relation to the Requisition, the identity of the Requisitioning Shareholders (and their network of affiliates) and the likelihood that the proposed resolutions would be successful[8] .

To cure their concerns and to seek to ensure that the composition of the Company's board was able to be voted upon in an "efficient, competitive and informed manner", the Takeovers Panel ordered the Requisitioning Shareholders to disclose their association by giving the Company (and ASX) a substantial holder notice. The form of this substantial holder notice was to be reviewed and approved by the Takeovers Panel.

Importantly, as the combined voting power of the Requisitioning Shareholders was less than 20%, their breach of section 671B did not also amount to a breach of the takeovers prohibition in section 606. If their combined voting power was greater than 20%, it is likely that the Takeovers Panel would have also ordered that the Requisitioning Shareholders not vote at the Requisitioned meeting and/or that they sell down their holdings to below 20%.

PRACTICAL CONSEQUENCES

Caution should be exercised by shareholders who are considering the making of a joint requisition in relation to the composition of a company's board of directors and who wish to avoid having to (or, if they wish to be in the best position to successfully) defend an allegation of association before the Takeovers Panel. As is usually the case however, the optimal strategy depends on the circumstances. For instance:

1. if the requisitioning shareholders are not (and do not expect to become) "associates" there is no statutory requirement for them to give a substantial holder notice to the company in question (and ASX)[9]
2. if the requisitioning shareholders may be or are concerned that they will be found to be "associates" they may wish to consider giving a substantial holder notice to the company in question (and ASX)[10] within two business days of the date of their requisition.

Combined voting power of less than 20%

Where the requisitioning shareholders collectively hold less than 20% of the shares in the company concerned, either of the above two approaches should (and even if the requisitioning shareholders do ultimately have to address any concerns that the Takeovers Panel may have) assist them in not breaching section 671B of the Corporations Act and/or becoming the subject of a declaration of unacceptable circumstances.

Combined voting power of more than 20%

Where the requisitioners collectively hold more than 20% of shares of the company in question, the declaration of unacceptable circumstances by the Takeovers Panel will almost certainly result in those shareholders being prevented from voting at the meeting they requisitioned and/or even being forced to sell down their holdings to below 20%.

The unanswered question in the wake of *Aguia Resources* is however whether the requisite disclosure under the substantial holder notice provisions of the Corporations Act by requisitioning shareholders who together hold more than 20% will be sufficient to avoid a declaration of unacceptable circumstances.

Until this regulatory uncertainty is resolved (perhaps by amending section 611 of the Corporations Act to make provision for requisitioning shareholders who disclose their combined voting power of 20% or more), it is arguable that the best (and indeed only) approach for requisitioning shareholders will be to (i) do all that they can to avoid the associate reference, (ii) carefully consider whether to disclose any potential association (ie for the avoidance of doubt) and (iii) seek to ensure that their combined voting power is as close to 5% as is practicable.

Footnotes

[1] Section 249D of the Corporations Act allows shareholders who hold at least 5% of the voting shares in a company to require the directors of that company to call and hold a meeting to consider the resolutions put forward by those shareholders.

[2] The Takeovers Panel may make a declaration of unacceptable circumstances under section 657A or an order under section 657D or 657E (but only following an application made under section 657C).

[3] As defined in section 9 of the Corporations Act.

[4] As defined in section 610 of the Corporations Act.

[5] When combined with certain "closely related parties", the Requisitioning Shareholders' aggregate voting power in the Company was found to have amounted to a maximum of approximately 13.12%.

[6] The commonality of the Requisitioning Shareholders' interests, actions or intentions with respect to the Company and their "structural links" amongst themselves and with other "closely related parties" was evidenced by prior meetings and email correspondence in which the Requisitioning Shareholders considered the (then) current and/or proposed composition of the board and their intentions in relation to the future operations of the Company.

[7] The Australian Securities and Investments Commission's (ASIC) submission in *Aguia Resources* was, however, more forthright in expressing ASIC's position in this regard. In ASIC's opinion "a joint requisition of a general meeting to appoint and remove the board of a company will invariably result in the joint requisitioners becoming associates (if they are not already)". This association will, in ASIC's view, arise even where the requisitioning shareholders are mindful of and therefore do all that they can to avoid the associate reference.

[8] The Takeovers Panel also referred to prior guidance given by ASIC in which ASIC stated that "a contravention of the substantial holder notice provisions (but not the takeovers threshold) of the Corporations Act is a sufficient basis upon which the Takeovers Panel may declare unacceptable circumstances where the contravention arises in the context of collective action regarding a proposed board spill".

[9] We expect that after Aquia Resources this approach will be more difficult to maintain.

[10] This strategy is not without risk. For example, if the requisitioning shareholders "concede" at the outset that they are associates, it will be less difficult for an applicant to the Takeovers Panel to establish that the requisitioners' combined holding is greater than 20% when their combined (and admitted) holding is aggregated with other holders who may also share their views in relation to the composition of the board of the company in question. Under the first approach however, any applicant to the Takeovers Panel would at least have to establish that the requisitioning shareholders are associated with each other before they could then seek to establish that the requisitioning shareholders are also associated with others in contravention of the 20% threshold in section 606.

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