BUDDLE FINDLAY

Schemes return in New Zealand

Grant Dunn

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Private equity firms in Australia and elsewhere have long been using schemes of arrangement to effect change of control transactions. Those looking to conduct a public to private transaction in New Zealand will welcome the news that schemes are now again considered suitable there.

Why were shareholder schemes not used in New Zealand?

For many decades schemes of arrangement have been available to effect change of control transactions in New Zealand but the strategy lost favour in 2005. In that year, Buddle Findlay advised SKY Network Television (SKY) on its merger with Independent Newspapers Limited (INL) by way of a scheme of arrangement whereby a special purpose vehicle (SPV) was formed to acquire all the SKY and INL shares in exchange for cash and scrip in the SPV. Because the SPV was acquiring more than 20% of the voting rights in a company required to comply with the New Zealand Takeovers Code (Code) a technical waiver from compliance with the Code was sought from the New Zealand Takeovers Panel.

The Panel was of the view that there should be no difference in the voting thresholds required for achieving a scheme and an offer (90%) and was only prepared to grant a waiver on that basis. In the end the scheme was simply drafted to provide for the cancellation of all SKY and INL voting rights before the SKY and INL shares were acquired (similar to a "cancellation scheme"). This resulted in a successful transaction requiring 75% class interest votes that did not breach the Code but from that point on the Panel viewed schemes with much suspicion as a structuring technique to avoid the Code. Legal advisers on future transactions were wary of suggesting schemes to their clients as that could lead to direct confrontation with the Panel in court and in the public arena.

A decade on, and with much water under the bridge, New Zealand has amended its Companies Act to follow the practice in Australia and allow the Panel to assist the court with supervision of schemes involving Code companies (Code companies generally being those that are listed or have more than 50 shareholders). The Panel now views schemes as a legitimate and valuable means for undertaking corporate transactions in New Zealand.

Benefits of using a scheme of arrangement

The principal advantages of using a scheme versus an offer under the Code are the same as those in Australia. Provided the requisite shareholder approval is obtained at the court-convened shareholder meetings (being at least 75% of the votes of each interest class entitled to vote and voting as well as a simple majority of votes of all shareholders entitled to vote) and the scheme has been sanctioned by the court, all shareholders of the target company are bound by the scheme whether they voted in favour for it or not.

There is no need to utilise the compulsory acquisition procedure under the Code to acquire the shares of the outstanding minority (a procedure which requires the bidder to hold at least 90% of the target company). The scheme route to full ownership clearly has a lower shareholder approval threshold than using a Code offer. For a bidder and its financers, this translates into greater deal certainty; an all or nothing result (generally known at the date of court sanctioning) with no possibility of a minority remaining; a potentially shorter time frame to obtain 100% (depending on how drawn out the compulsory acquisition procedure under the Code could be); less concern for lost or untraceable shareholders that form a "dead share register"; and more flexibility to deal with any target company's option scheme, convertible notes or any novel structuring issues.

For the banks that are lending acquisition funding to the bidder, a scheme provides for a much simpler single funding date and security being granted over the whole target group without any opposition to financial assistance from minority shareholders.

Another advantage of using a scheme is that it does not have a rigid timetable set down by the Code. The Code contains very specific timeframes and in particular only allows 120 days from the date of the offer for any regulatory conditions to be satisfied. In New Zealand, it is well known that seeking consent from the Overseas Investment Office (OIO) to a transaction involving the acquisition of "sensitive land" (certain agricultural land and land next to the foreshore/seabed for example) by a foreign bidder can cause timetable delays. Unfortunately, the OIO approval process is not as streamlined as that of the Foreign Investment Review Board (FIRB) in Australia. With OIO consents for sensitive land transactions taking at least three months and typically longer, a bidder making a takeover offer will find that the Code timetable does not cater well for satisfaction of regulatory conditions and the bidder effectively runs out of time to declare the offer unconditional. If the maximum offer period under the Code is exceeded from having to wait upon an OIO decision, the offer will lapse and a new offer (with all its legal documentation) will need to be launched. A scheme, on the other hand, with its flexible timetable caters well for conditions such as OIO consent that may take some time to satisfy. A foreign bidder requiring either OIO consent for acquiring sensitive land or, say, competition or anti-trust approvals would be well advised to employ a scheme.

The recently announced (15 February 2016) takeover by way of scheme of arrangement by Allnex Belgium SA/NV (a portfolio company of Advent International Corporation) for NZX/ASX listed Nuplex Industries is a case in point, requiring numerous anti-trust approvals and clearances around the world, including within the US and China. A Code offer would not have been practical given the timeframes for securing such a large number of consents.

What's unique in New Zealand schemes?

Little local case law

Because schemes have been relatively uncommon in New Zealand, unlike Australia, both the Panel and the courts do not have a rich history in considering shareholder schemes. Therefore, before taking matters for granted as common practice, a bidder may need to be prepared to advance their case for dealing with any complicated issues first with the Panel and then with the court, based upon legal precedent in offshore common law systems (in particular in Australia and England) as support. Certainly, local legal advisers with a good working knowledge of scheme case law will be a pre-requisite in deciding on the bidder's legal team.

No headcount test

The approval threshold in Australian schemes is generally a resolution passed by a majority in number of the shareholders in the class present and voted for and passed by 75% of the votes cast. New Zealand legislation does not contain a similar "headcount test" but it does have an additional requirement that at least a simple majority of all shares must be voted for in favour. As a result, unlike Australia, a large group of shareholders by number but with a small voting percentage, cannot disproportionately tilt the balance of power. Any concerns about vote splitting do not apply in New Zealand.

Lock-ups

Despite the difference in wording between the Australian Corporations Act and the New Zealand Companies Act, the position for pre-bid voting agreements ends up the same in New Zealand. A bidder and major shareholders can enter into voting agreements to vote in favour of the scheme up to an aggregate 20% of the voting shares (the New Zealand Takeovers Code prohibits the "controlling" of voting rights in excess of 20%). Beyond that level it is possible for shareholders to publicly indicate their intention to vote in favour of their holding in the absence of a superior proposal, but publically announced statements of intention are not a common feature in New Zealand deals.

Where a fundamental difference between Australia and New Zealand arises, is in deciding whether to utilise an offer or scheme when the bidder is aware of pending key shareholder support. The Australian Corporations Act restricts a bidder obtaining a relevant interest, or reaching any agreement, arrangement or understanding as to voting or disposal in respect of more than 20% of the target company. In contrast, last year the Panel in New Zealand relaxed its strict view of pre bid agreements (or lock-up agreements) creating an automatic association between the bidder and the major shareholder so that now, provided the lock-up agreement purports to merely accept a takeover offer and does not pass control of voting rights until the takeover offer is unconditional, it will not create an association between bidder and shareholder. This leaves a bidder open to pursue numerous lock-ups well in excess of 20% of the target shareholder base. It is therefore possible in New Zealand takeovers for the bidder to have locked up more than, say, 50% of the target shareholders prior to the offer being announced.

Given the greater extent of this strategic tool under the offer route, a bidder must carefully analyse the target company's share register and decide what gives greater deal certainty - lock-ups for greater holdings under the traditional Code offer route and a 90% threshold to commence the squeeze-out process versus a scheme of arrangement with a 20% cap on lock-ups and a 75% threshold to effect the squeeze out.

Failed bid costs

Many offshore bidders are surprised to learn that the New Zealand Takeovers Code provides that the target company may recover from the bidder any expenses properly incurred by the target company (and its directors) in relation to a takeover notice or offer. While any bidder dislikes its own failed bid costs, stumping up for the costs of the target's lawyers, accountants, financial advisors, analysts, public relations experts, printers and the independent adviser can very much leave a bidder with a bad impression of the New Zealand takeover experience.

Both Crescent Capital and the Canada Pension Plan Investment Board had well publicised disagreements with target company boards (Abano Healthcare and Auckland Airport respectively) in 2008 over the level and make-up of such costs leading the Panel to publish a guidance note on the matter. The advantage of a scheme is that this provision of the Code will not apply and, in the absence of anything to the contrary in the scheme implementation deed, costs between the bidder and the target company will lie where they fall. While break fees and reverse break fees that seek on one level to apportion some of these costs are frequently used in the public M&A landscape in Australia, these are less common in New Zealand. That position could, however, well change as invariably schemes, with their heavily negotiated outcomes, seem to naturally facilitate discussion between bidder and the target company boards on a number of topics such as this.

The future for New Zealand public M&A

With a wide range of possible benefits, we expect offshore private equity bidders who are well versed in using schemes of arrangement in markets such as the UK, Australia, Canada, Hong Kong, Singapore, Malaysia, India and even the BVI, Bermuda and Cayman Islands, to name a few, to favour a scheme when planning a public to private transaction in the New Zealand market.

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Auckland

188 Quay Street
Auckland 1010

PO Box 1433
Auckland 1140
New Zealand

P: +64 9 358 2555
F: +64 9 358 2055

Wellington

Aon Centre
1 Willis Street
Wellington 6011

PO Box 2694
Wellington 6140
New Zealand

P: +64 4 499 4242
F: +64 4 499 4141

Christchurch

83 Victoria Street
Christchurch 8013

PO Box 322
Christchurch 8140
New Zealand

P: +64 3 379 1747
F: +64 3 379 5659