Guidance Note

UPSTREAM ACQUISITIONS

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TAKEOVERS PANEL
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Contents

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This Guidance Note sets out the Panel's policy for dealing with the impacts of the Takeovers Code on upstream acquisitions. If an upstream company holds or controls voting rights in a downsteam Code company, then the acquisition of effective control of that upstream company may trigger obligations under the Code.

This Guidance Note has been updated to clarify the Panel's approach to the Purpose Test and to include an example.

See Appendix A for the Panel's Upstream Exemption Policy.

1 Introduction

1.1 This Guidance Note sets out the Panel's policy for dealing with the impacts of the Takeovers Code on upstream acquisitions. To keep the policy manageable, this Guidance Note deals with "base case" scenarios. Every case that comes before the Panel will need to be considered on its own merits and circumstances.

2 What is an upstream acquisition?

2.1 An upstream acquisition is an acquisition that occurs in New Zealand or overseas, that results in the acquirer of the upstream target becoming a controller of voting rights in a New Zealand Code company.[1] This acquisition of control occurs because the upstream target holds or controls voting rights in that Code company and that asset (i.e., the voting rights) is acquired as part of the acquisition of the upstream target entity.

2.2 The acquisition of control of voting rights in a downstream Code company may be incidental to the acquirer's purpose of acquiring the upstream target. However, the acquisition of an upstream entity can also be effected for the purpose of indirectly acquiring control of an interest in the downstream Code company.

3 Application of the Code

3.1 Where:

(a) an upstream target entity holds or controls more than 20% of the total voting rights in a New Zealand Code company (the **Downstream Voting Rights**);and

(b) control of the upstream target is acquired by the upstream acquirer (usually on completion of the upstream transaction),

then:

(c) the upstream acquirer will become the effective controller of the Downstream Voting Rights; and

(d) the upstream acquirer must comply with the Code in respect of that downstream acquisition.[2]

3.2 The question of whether an upstream acquisition results in an upstream acquirer becoming an effective controller of the Downstream Voting Rights is not always certain:

(a) There are clear cases where effective control over the Downstream Voting Rights will be achieved (for example, the takeover succeeds and the upstream acquirer obtains 100% control of the upstream entity).

(b) The Panel assumes that any acquisition of more than 50% of the voting rights of an upstream target would result in the upstream acquirer obtaining effective control over the Downstream Voting Rights. However, an

[1] See meaning of Code Company in rule 3A of the Takeovers Code.
[2] Similarly, Code compliance will be required if Downstream Voting Rights comprise 20% or less of the total voting rights of the Code company, but, when aggregated with other voting rights held or controlled by the upstream acquirer or its associates, would exceed 20%.

upstream acquirer may be able to establish that the Panel's assumption about obtaining control would not apply to its specific circumstances.

(c) If the upstream acquirer acquires 50% or less of the voting rights of the upstream target, the extent to which it will gain control of the Downstream Voting Rights will depend on the circumstances.

Prior shareholder approval or prior takeover offer

3.3 In order to comply with the Code, before the upstream acquirer gains control of the upstream target (and therefore of the Downstream Voting Rights), the acquirer must have either:

(a) obtained approval for the upstream acquisition by the downstream Code company's shareholders by way of ordinary resolution under rule 7(c) of the Code; or

(b) completed a takeover of the downstream Code company under rule 7(a) of the Code.

3.4 Where the upstream acquirer made a takeover offer for the downstream Code company, it would need to do so contemporaneously with, or in advance of, its acquisition of the upstream target. It would, in order to comply with the Code, need to have included in the upstream takeover offer appropriate conditions to ensure that it did not gain control of the upstream target, and, therefore, of the Downstream Voting Rights, until the takeover offer for the downstream Code company succeeded. Likewise, downstream shareholder approval of the upstream acquisition, under rule 7(c) of the Code, would have to have been completed before the upstream acquisition became unconditional.

3.5 Both compliance options are impracticable, if not impossible, in some cases. The alternative to complying with the Code's requirements is to obtain an exemption from those requirements. This guidance note provides guidance to the market as to how the Panel is likely to exercise its discretion to grant exemptions in such circumstances.

4 Application for exemption

4.1 The Panel will consider applications for exemptions from the Code in relation to upstream acquisitions on a case-by-case basis.

4.2 The exemption process is set out below and illustrated in the diagram at Appendix A of this guidance note. The purpose of this guidance note is to set out the Panel's general policy in respect of upstream acquisitions. It does not attempt to address every possible scenario that might occur. Accordingly, this guidance note sets out the "base-case".

Unconditional exemption

4.3 The Panel will normally grant an unconditional exemption from rule 6(1) of the Code for an upstream acquirer, where the upstream acquisition would result in the upstream acquirer becoming the controller of more than 20% of the total voting rights in a downstream Code company, if acquiring control of the Downstream Voting Rights would not reasonably be regarded as a significant purpose of the upstream acquisition (**Purpose Test**).

4.4 There are two key enquiries in relation to the Purpose Test:

(a) First, is the value of the securities to which the Downstream Voting Rights attach (the **Downstream Parcel**)[3] less than 25% of the enterprise value of the upstream target (or such other valuation methodology that the Panel considers may be appropriate in the circumstances) (the **Value Test**).[4]

(b) As a secondary question, is the upstream target listed on a "recognised exchange" as described below (the **Listing Standard**).

4.5 If the Value Test and Listing Standard are met, then the Purpose Test will be prima facie satisfied. However:

(a) The Value Test and Listing Standard are only proxies for purpose.

(b) If the Panel considers that a significant purpose of the upstream acquisition is to acquire control of the Downstream Voting Rights, the meeting of the Value Test and/or the Listing Standard will be disregarded.[5]

(c) If the Value Test is met but the Listing Standard is not met, the Panel may still consider that the Purpose Test is met, but this may affect the conditions that may attach to an exemption.

4.6 Where the value of the Downstream Parcel is more than 25% of the enterprise value of the upstream target, it is possible that the failure to meet the Value Test may be disregarded if the Panel is satisfied that it is not a significant purpose of the acquisition to acquire control of the Downstream Voting Rights.

4.7 "Recognised exchanges" are New Zealand Exchange Limited and foreign exchanges in jurisdictions with a comparable level of investor protection to New Zealand. The Panel has identified the following foreign exchanges to be "recognised exchanges": the Australian Securities Exchange, Deutsche Börse AG, Euronext Amsterdam NV, Euronext Paris SA, Italian Exchange SpA, JSE Securities Exchange South Africa, Kuala Lumpur Stock Exchange, London Stock Exchange plc, The NASDAQ Stock Market Inc, New York Stock Exchange Inc, Singapore Exchange Limited, The Stock Exchange of Hong Kong Limited, Swiss Stock Exchange, Tokyo Stock Exchange, The Toronto Stock Exchange Inc.

Conditional exemption

4.8 If the Purpose Test is satisfied, the Panel is likely to grant an exemption which will usually be subject to no (or very limited) conditions. Specifically:

(a) Where both aspects of the Purpose Test are met, the exemption will likely be unconditional.

(b) Where the Listing Standard is not met, but the Purpose Test is nonetheless satisfied, the exemption will likely include a condition that the material terms of the upstream acquisition are disclosed to shareholders of the downstream Code company on or before the date on which the upstream acquirer increases its control of Downstream Voting Rights.

4.9 If the Purpose Test is not satisfied, the Panel will most likely not grant an unconditional exemption.

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[3] The starting point for valuing the Downstream Parcel will typically be a suitable VWAP figure. However, VWAP may not be appropriate in all circumstances. Examples include where the Code company is not listed or where it is not appropriate to attach a minority discount to the Downstream Parcel (for example, where the Downstream Parcel carries effective control over the Code company).

[4] For the purposes of determining the enterprise value, debt in the downstream company consolidated in the upstream company is excluded. Where a company is listed, an assessment of its enterprise value will involve an assessment of its market capitalisation. If a company is not listed, the Panel will decide the appropriate methodology.

[5] Other factors that may indicate an upstream acquirer's purpose include:

(a) public statements that indicate a purchaser's intentions one way or the other;

(b) the fact of a previous offer having been made for the Code company (which could indicate that the downstream acquisition was a significant purpose);

(c) any association or aggregation of voting interests or entitlements in the downstream Code company, caused by the upstream acquisition (which will likely suggest a significant purpose to acquire the voting rights); or

(d) cross shareholdings or board memberships between any of the offeror, the upstream target, the downstream Code company, and their associates (again, this could indicate that a significant purpose was to acquire the downstream Code company voting rights).

4.10 However, the Panel will normally grant a conditional exemption in these circumstances. The exemption would likely be subject to the condition that the upstream acquirer elects, and undertakes, one of the following options (together, the **Compliance Options**), being to either:

(a) decrease the upstream target's holding or control of securities carrying voting rights in the downstream Code company to 20% or less by no later than six months after the upstream acquisition becomes unconditional, and ensure that pending the decrease occurring the upstream target does not exercise any more than 20% of the total voting rights (**Control Reduction Option**);[6] or

(b) make a follow-on offer for the rest of the shares in the downstream Code company within 40 working days after the upstream acquisition becomes unconditional (the **Follow-on Offer Option**).

4.11 It will generally be a requirement that the election of the Compliance Option be notified to the Panel and to the downstream Code company (and, if either of the upstream target or the downstream Code company has its ordinary shares quoted on a New Zealand registered exchange, notified to the registered exchange) no later than either:

(a) 10 working days after the follow-on offer price is determined (see below for details about the determination of the follow-on offer price); or

(b) the working day after the upstream acquisition becomes unconditional.

4.12 This timing allows the election of the Compliance Option to be made after the follow-on offer price is determined. However, the election of a Compliance Option could be made at any time in advance of the follow-on offer price being determined.

Requirements of the Control Reduction Option

4.13 If the Control Reduction Option is elected, the upstream acquirer must undertake to the Panel that it will procure the upstream target to decrease its holding so that the upstream acquirer would hold or control no more than 20% of the total voting rights in the downstream Code company after the decrease. This must normally be achieved no later than six months after the upstream acquisition becomes unconditional. The upstream acquirer must also undertake to the Panel that, pending the decrease occurring, it will procure the upstream target to not exercise any voting rights in the Code company above the permitted 20% level. If the shares are divested, any acquirer(s) of the shares must themselves comply with the Code. That means, for example, that the upstream acquirer could not sell the shares to any associates unless the associates obtained the approval of the Code company shareholders, in accordance with rule 7(c) of the Code.

Requirements of the Follow-on Offer Option

4.14 The consideration for the follow-on offer must be cash (or include a cash alternative) and must be determined as follows:

(a) If the Panel is satisfied that the price effectively being offered to the upstream target for its shares in the downstream Code company can be clearly and accurately determined from the upstream offer consideration (the **see-through price**), the follow-on offer consideration will be not less than the see-through price. Only in rare cases will the see-through price be able to be clearly and accurately determined, for example, where the only assets of the upstream target were the shares in the downstream Code company.

[6] This assumes that the upstream acquirer did not hold or control any voting rights in the downstream Code company prior to the upstream acquisition.

(b) Where the see-through price cannot be clearly and accurately determined, the follow-on offer consideration will be not less than the fair and reasonable value per share,[7] as determined by an independent expert that is appointed by the Panel.

4.15 In relation to the Follow-on Offer Option, the following additional conditions of exemption would apply:

(a) The offeror must pay the reasonable fees, costs and expenses of the independent expert in relation to its determination of the follow-on offer price.

(b) The offeror must include with the offer document that is sent to shareholders for the follow-on offer a copy of the independent expert's valuation and an explanation of how the follow-on offer price was derived.

(c) Any other terms and conditions of the follow-on offer, included by the offeror in the offer document, must be in a form approved by the Panel.

4.16 The other terms and conditions of the follow-on offer (referred to in paragraph 4.15(c), above) that the Panel may approve, could include:

(a) the usual conditions of takeover offers that are made pursuant to the Code (the Panel would need to have approved the wording of these and all other conditions); and

(b) that the requisite regulatory approvals (such as from the Overseas Investment Office or Commerce Commission) are obtained, and that the upstream acquirer will use its best endeavours in good faith to obtain all such approvals.

4.17 However, there could be no minimum acceptance condition included in the follow-on offer, other than that stipulated by rule 23 of the Code.

4.18 Also applicable to the follow-on offer conditions is rule 25(1) of the Code, together with the Panel's guidance on restrictive conditions, set out in the *Guidance Note on Offer Documents*.

4.19 It would not be a condition of the exemption granted by the Panel that a follow-on offer must succeed.

Appointment of an independent expert

4.20 The independent expert would be appointed by the Panel as follows:

(a) The upstream acquirer would request that the Panel appoints an independent expert.

(b) The request must include a list of the advisers from whom the upstream acquirer has already received advice in relation to the upstream acquisition and the resulting downstream acquisition. The upstream acquirer should not make any suggestions as to who it thinks would be appropriate for appointment by the Panel. However, the upstream acquirer should also advise the Panel of any firms that it considers might be conflicted, and why it considers them likely to be conflicted.

(c) The Panel would then undertake a closed tender process inviting applications from experts that it considers suitable. The Panel would approach those experts on a confidential basis. The independent expert would be selected on the basis of independence and appropriate qualifications and experience. The Panel would also take each expert's quoted fees into account when selecting the expert for appointment.

4.21 The appointment process is consistent with the appointment process for an independent expert under rule 57 of the Code, which can be found on the *Guidance Note on Independent Advisers*.

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[7] The fair and reasonable value per share must be calculated by:
(a) first assessing the value of all the shares in each class; and
(b) then allocating that value pro rata among all the shares of that class.

4.22 At least 10 working days should be allowed for the appointment process and up to a further four weeks for the valuation to be undertaken by the appointed expert. The expert will undertake a valuation on the basis of all available information at the time of the valuation.

4.23 A follow-on offer must be made within 40 working days after the upstream acquisition becomes unconditional. Accordingly, it would be advisable for the upstream acquirer to approach the Panel for an exemption as early as possible in the acquisition (or pre-acquisition) process. If a conditional exemption is granted to the upstream acquirer by the Panel, requiring the upstream acquirer to elect a Compliance Option, it may be pragmatic to request at that time that the Panel appoints an independent expert. This would help to ensure that the compliance timeframes were able to be comfortably met. The Panel will keep confidential any exemptions granted, where it is proper to do so on the ground of commercial confidentiality.

Market disclosure

4.24 The market for shares in the downstream Code company must be adequately informed in relation to the upstream acquisition. The upstream acquirer must notify its election of a Compliance Option to the Panel and to the downstream Code company, no later than either:

(a) 10 working days after the follow-on offer price is determined; or

(b) the working day after the upstream acquisition becomes unconditional.

4.25 If the Follow-on Offer Option is elected, the notification must include full details of both the upstream and downstream acquisitions, including the timing and consideration for the acquisitions. (The consideration for the downstream acquisition must be disclosed only if that consideration has been determined at the time of the announcement.) If the upstream target or the downstream company is listed on a New Zealand registered exchange, the notification must also be given to the New Zealand registered exchange at the same time that it is given to the Panel and to the downstream Code company.

5 Rule 64 of the Code – prohibition on misleading or deceptive conduct

5.1 Rule 64 of the Code prohibits misleading or deceptive conduct in relation to Code-regulated transactions or events.[8]

5.2 Any statements, actions or other conduct by any person in relation to the downstream Code company (or potentially the upstream acquisition) would be subject to the rule 64 prohibition.

5.3 Particular care should be taken over "last and final statements". For example, if the upstream acquirer were to state that it was going to elect the Control Reduction Option, that would constitute a last and final statement that is subject to rule 64. The Panel would likely find that rule 64 had been breached if the upstream acquirer did not then elect the Control Reduction Option.

5.4 Likewise, shareholders, directors and any other persons are subject to the rule 64 prohibition against misleading or deceptive conduct.

5.5 The Panel's policy on last and final statements is set out in the *Guidance Note on Misleading or Deceptive Conduct*.

[8] Rule 64 provides that:
(1) A person must not engage in conduct that is-
(a) conduct in relation to any transaction or event that is regulated by [the] Code; and
(b) misleading or deceptive or likely to mislead or deceive.
(2) A person must not engage in conduct that is-
(a) incidental or preliminary to a transaction or event that is or is likely to be regulated by [the] Code; and
(b) misleading or deceptive or likely to mislead or deceive.

6 Case Studies

Case study: AMP / AXA Asia Pacific/ AMP NZ Office

6.1 In 2011, the Panel granted an exemption from rule 6(1) of the Code to AMP Limited (and certain of its related entities) (**AMP**) in relation to the proposed merger of AMP with the Australasian business of AXA Asia Pacific Holdings Limited (**AXA**). One component of AXA's business was a funds management operation that held approximately 2.8% of the shares in AMP NZ Office Limited (**ANZO**), a NZX-listed Code company. At the time of the proposed merger, AMP (through a subsidiary) already held or controlled a percentage of voting rights in ANZO that was, when aggregated with one of AMP's associates, slightly more than 20%. Therefore, the merger would have resulted in AMP becoming the holder or controller, through the upstream acquisition of AXA, of an increased percentage of voting rights in ANZO in breach of rule 6(1) of the Code.

6.2 The exemption involved the application of the Value Test as a proxy for the Purpose Test (see paragraph 4.4(a) above). The Panel decided that the proposed transaction fell squarely within the policy for an unconditional exemption under the Guidance Note. In terms of the Value Test, the value of AXA's holding in ANZO represented less than 0.1% of AXA's business and, following the merger, the holding would equate to approximately 0.2% of AMP's business. Therefore, in each case the value of the interest held by the upstream company in ANZO as a result of the merger was significantly less than the 25% threshold set out in the Guidance Note.

6.3 See the exemption notice.

Case study: Opus International Consultants Limited

6.4 The Panel approved the granting of an unconditional exemption from rule 6(1) of the Code in relation to the proposed acquisition of 100% of the voting rights in Opus Group Berhad (**OGB**) by Faber Group Berhad (**Faber**) (both Malaysian companies) (**Proposed Transaction**) (see the diagram below). In granting its exemption, the Panel applied its policy for dealing with upstream acquisitions.

6.5 The Proposed Transaction had downstream implications as regards the control of voting rights in Opus International Consultants Limited, a New Zealand Code company (**Opus NZ**).

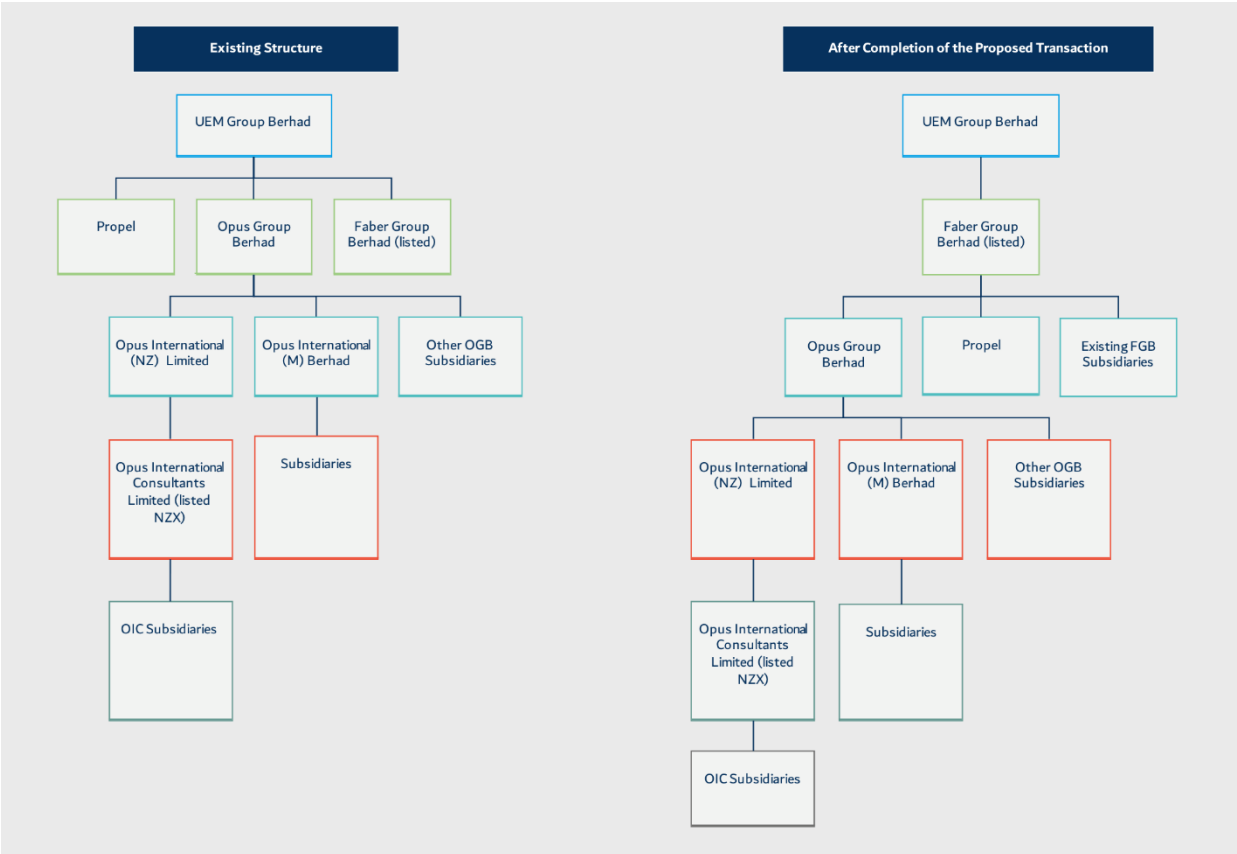
6.6 The acquisition of OGB by Faber would (indirectly, through its wholly owned subsidiaries) result in Faber becoming the controller of more than 20% of the voting rights in Opus NZ and, as such, required compliance with rule 6 of the Code. In the absence of an exemption, Faber would have had to obtain the approval of Opus NZ's shareholders for the Proposed Transaction, by ordinary resolution.

6.7 OGB was not listed on a recognised exchange, and therefore did not meet the Listing Standard. However, the Panel took into account the fact that Faber was listed on a recognised exchange, and information regarding the Proposed Transaction had been disseminated through, and was available on, that exchange.

6.8 The Proposed Transaction did not meet the Value Test, but the Panel considered that a reasonable person would not regard acquiring control of the voting rights in Opus NZ as a "significant purpose" of the Proposed Transaction. In reaching this view, the Panel noted that the Proposed Transaction was at its most basic a consequence of the "reverse takeover" of Faber by UEMG Group Berhad (the group parent).

6.9 See the exemption notice.

Opus International Consultants Structure



Case study: Terra Vitae Vineyards Limited

6.10 Terra Vitae Vineyards Limited (**TVL**) was an unlisted Code company whose shares were traded on the Unlisted Securities Exchange (**USX**). Villa Maria Estate Limited (**VMEL**) held 21.89% of the shares in TVL (the **VMEL Parcel**). TVL and VMEL were parties to a long-term grape supply and vineyard management agreement (the **Agreement**).

6.11 VMEL was wholly owned by FFWL Limited (In Receivership) (**FFWL**). Indevin Group Limited (**IGL**) proposed to acquire 100% of the shares in VMEL from FFWL, which would result in IGL and certain of its upstream parties gaining effective control over the VMEL Parcel. Accordingly, the proposed acquisition was subject to the Code.

6.12 VMEL was not listed on a recognised exchange, and so did not meet the Listing Standard. However, the Panel was satisfied that acquiring control of VMEL's holding in TVL was not a significant purpose of the proposed transaction, for two reasons. Firstly, the Value Test was met, as the value of the VMEL Parcel represented a small percentage of VMEL's enterprise value, falling significantly under the 25% threshold. Secondly, VMEL's control of TVL flowed largely from the Agreement rather than its holding in TVL.

6.13 The Panel granted IGL and certain of its upstream parties an exemption from rule 6(1) of the Code subject only to a disclosure condition, to provide for TVL's shareholders to be appropriately informed of the material terms of the upstream acquisition.

6.14 See the exemption notice.

APPENDIX A
The Panel's Upstream Exemption Policy