

**CLASS EXEMPTION
FOR TRUSTEES OF FAMILY TRUSTS**

**A CONSULTATION PAPER ISSUED BY THE
TAKEOVERS PANEL**

Takeovers Panel
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INTRODUCTION

1. The Panel is considering whether to grant a class exemption from rule 6(1) of the Takeovers Code (the “Code”) relating to:
 - (a) the appointment of new trustees to family trusts who are caught by rule 6(2)(b); and
 - (b) the reduction in the number of trustees of family trusts who are caught by rule 6(2)(c)

on the basis that exemptions from rule 6(1) for trustees in these circumstances are commonly granted by the Panel as these transactions are not intended to be caught by the Code.

2. This paper discusses the Panel’s current approach in granting specific exemptions from rule 6(1) of the Code for trustees, the appropriateness of granting a class exemption and the possible terms and conditions of a class exemption.

Request for comments on this paper

3. The Panel invites submissions on the issues raised in this paper and the options identified for addressing the issues.
4. The closing date for submissions is **Friday 13 April 2012**.
5. Submissions should be sent to the Takeovers Panel for the attention of Heather McCaskill–

By email - heather.mccaskill@takeovers.govt.nz

By post- Takeovers Panel
Level 3, Solnet House
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Official Information Act

6. Any submissions received are subject to the Official Information Act 1982. The Panel may make submissions available upon request under that Act. If any submitter wishes any information in a submission to be withheld, the submission should contain an appropriate request (together with a clear identification of the relevant information and the reasons for the request). Any such request will be considered in accordance with the Official Information Act 1982.

IDENTIFICATION OF THE PROBLEM

Status Quo

7. The Panel has granted numerous exemptions from rule 6(1) of the Code for trustees of family trusts that hold or control 20% or more of the voting rights in a Code company in respect of changes in trustees resulting from:
 - (a) the appointment of new trustees to family trusts who are caught by rule 6(2)(b); and
 - (b) the reduction in the number of trustees of family trusts who are caught by rule 6(2)(c) (see Appendix A for a list of Exemption Notices).
8. The Panel's approach has been to review each transaction on a case by case basis, so that it can be satisfied that in the relevant circumstances the change of trustees relates to a bona fide reorganisation of a family trust or other investment vehicle as the Code is not intended to inhibit these sorts of transactions.

Rule 6(2)(b): appointment of new trustees

9. Rule 6(2)(b) of the Code states that if -

a person or persons together hold or control voting rights and another person joins that person or all or any of those persons in the holding or controlling of those voting rights as associates, the other person is deemed to have become the holder or controller of those voting rights.
10. This means that a newly appointed trustee, as an associate of the existing trustees, will be deemed to have become the holder or controller of the same shares that the existing trustees currently hold and control in the Code company.
11. Over the years the Panel has considered a number of exemption applications under rule 6(2)(b) in respect of the appointment of new trustees to family trusts. In each case the Panel considers the terms of the relevant trust deed, is informed of the identity of the relevant trustees and weighs up any effect on the shareholders of the Code company.
12. Recent examples of such exemptions include:
 - (a) *Takeovers Code (Delegat's Group Limited) Exemption Notice 2010*: The trustees of the Protection Trust ("Protection Trust") held or controlled 33.8% of the voting rights in Delegat's Group Limited ("DGL"). It was proposed to appoint Mr Bob Wilton as a trustee to replace a retiring trustee. Mr Wilton was joining with the other trustees as an associate in the holding or controlling of more than 20% of the voting rights in DGL. The Panel granted Mr Wilton an unconditional exemption in respect of his appointment as a trustee to the Protection Trust.
 - (b) *Takeovers Code (Michael Hill International Limited) Exemption Notice 2010*: The Boxer Hill Trust, Quinten Trust and Michael Hill International Share Trust ("Michael Hill Trusts") in aggregate held or controlled 47.61% of the voting rights in Michael Hill International Limited ("MHI"). On August 2009,

Veritas Hill Limited (“Veritas”) was appointed as a trustee of each of the Michael Hill Trusts thereby joining the other trustees as an associate in the holding or controlling of more than 20% of the voting rights in MHI. The Panel granted Veritas an unconditional retrospective exemption in respect of its appointment to each of the Michael Hill Trusts.

Rule 6(2)(c): reduction in the number of trustees

13. Rule 6(2)(c) of the Code provides that if -

voting rights are held or controlled by a person together with associates, any increase in the extent to which that person shares in the holding or controlling of those voting rights with associates is deemed to be an increase in the percentage of the voting rights held or controlled by that person.
14. This means that if a person who is associated with others, in relation to a parcel of voting rights, increases the extent to which he or she shares in the holding or controlling of the voting rights, the associate will be deemed to have increased their percentage of voting rights in the Code company.
15. Where there has been a reduction in the number of trustees of private family trusts, the Panel has consistently treated the continuing trustees as being caught by rule 6(2)(c), on the basis that:
 - (a) trustees are likely to be associates for the purposes of the Code due to having an “ownership relationship” within the meaning of rule 4(1)(d) of the Code:¹ and
 - (b) the reduction of the number of trustees equates to an increase for each of the continuing trustees in the extent to which they share in the holding or controlling of voting rights with the continuing associated trustees. This is because each of the continuing trustees will have to come to agreement on matters relating to trust decisions with fewer trustees thereby increasing the influence of each continuing trustee on the decision making process. In that sense, the extent to which each of the continuing trustees shares in the control of the voting rights will increase.
16. As with exemptions under rule 6(2)(b), each application is considered on its facts, namely, the terms of the relevant trust deed, the identity of the relevant trustees and any effect on the shareholders in the Code company.
17. The Panel has granted numerous exemptions in relation to the reduction in the number of trustees of family trusts. Examples include:
 - (a) *Takeovers Code (Speirs Group Limited) Exemption Notice 2011*: The trustees of the R N Speirs Trust and the D P Speirs Trust held 50.23% of the voting rights in Speirs Group Limited (“Speirs”). Some of the older trustees of the R N Speirs Trust were retiring. Although there was no increase in the continuing trustees’ shareholding in Speirs, nevertheless they were caught by rule 6(2)(c)

¹ Rule 4(1)(d) of the Code provides that a person will be an associate of another person if –
the persons have a business relationship, personal relationship, or an ownership relationship such that they should, under the circumstances, be regarded as associates.

on the basis that the reduction of the number of trustees in the R N Speirs Trust equated to an increase for each of the continuing trustees in the extent to which they shared in the holding or controlling of voting rights. The Panel granted the continuing trustees of the R N Speirs Trust an exemption from rule 6(1) of the Code in respect of any deemed increase in their control of Speirs resulting from the reduction in the number of trustees of the R N Speirs Trust.

- (b) *Takeovers Code (New Zealand Experience Limited) Exemption Notice 2009:* The Trustees of the George R Gardiner Estate Trust (“Estate Trust”), Arthur Scace, Anthony Arrell and Helen Gardiner controlled 74.9% of the voting rights in New Zealand Experience Limited (“NZE”) through a chain of wholly owned subsidiaries. In July 2008 Mrs Gardiner passed away. The reduction in the number of trustees on the death of Mrs Gardiner increased the extent to which the continuing trustees shared in the control over the NZE voting rights with each other. Accordingly, rule 6(2)(c) deemed both of them to have become the controller of an increased percentage of voting rights in NZE and so Messrs Scace and Arrell appeared to have inadvertently breached the Code. The Panel granted the continuing trustees a retrospective exemption from rule 6(1) of the Code in respect of any deemed increase to their voting control in NZE resulting from the reduction in the number of trustees of the Estate Trust.

18. Exemption applications resulting from changes to trustees of family trusts, whether through a new appointment or through a reduction in the number of trustees, have all had the following features in common:

- (a) the trustees are trustees of a private family trust established to mainly benefit family members;
- (b) the trustees are family members or persons related to family members or are their advisers, and the beneficiaries are family members;
- (c) the trust deeds have standard provisions, including:
 - (i) Only the settlor (or any person whom the settlor has appointed to exercise the powers to remove and appoint new trustees) has powers to remove and appoint new trustees;
 - (ii) the trustees must act unanimously and therefore the voting rights in a Code company are exercised by trustees together;
- (d) the change in the number of trustees through appointments of new trustees or the retirement of existing trustees is due to a bona fide reorganisation of the trust’s affairs;
- (e) the reorganisation does not involve any increase in the percentage of voting securities in the Code company held or controlled by the trustees; and
- (f) any breach of the Code due to an unexpected reduction in the number of trustees is unintentional and most likely unavoidable.

19. In these circumstances the Panel has taken a consistent approach and has considered the exemptions in these cases to be appropriate and consistent with the objectives of the Code because:

- (a) the appointment of a new trustee or a reduction of the number of trustees relates to a reorganisation of a private family trust or an event outside the control of the trustees and the Code is not intended to inhibit the restructuring of family trusts that have no real effect on the shareholders of a Code company;
- (b) in the case of a trustee exiting the trust, although a reduction in the number of trustees will result in the continuing trustees each being deemed to increase their holding or controlling of voting rights in a Code company, the Code is not intended to regulate these changes to the trustees of family trusts;
- (c) in the case of a person being appointed as a trustee, the shareholders of the Code company would not be disadvantaged in not having the opportunity to vote on a trustee's appointment as trustee of the trust, as it would not have any real effect on those shareholders; and
- (d) the exemption avoids unnecessary compliance costs that would be incurred if it were not granted.

The Problem

- 20. These types of changes of trustees relate to a bona fide reorganisation of a private family trust or an event outside the control of the trustees. They involve no increase in voting control in the Code company on behalf of the trust. They have no real effect on the shareholders of the Code company. In cases where there has been a sudden and unexpected reduction in the number of trustees for example due to death or disability, the consequential breach of the Code is unintentional and even unavoidable.
- 21. It can take up to six weeks for the exemption process to be completed through to gazetting of an exemption notice. Applications to the Panel for these types of exemptions can cost an applicant in the region of \$4,000 to \$10,000 in fees charged by the Panel, depending on the complexity of the issues.² In addition to the Panel's fees, applicants will be likely to have to pay for the fees charged by their advisers. From the perspective of a private family trust, the impact of the exemption process, in circumstances where the Code is not intended to apply, may be considered a relatively significant burden.

POLICY OBJECTIVE

- 22. The Panel's policy objective is the maintenance of a proper relationship between the costs and benefits of compliance with the Code, while ensuring that the shareholders of Code companies are treated fairly.

OPTIONS AND ANALYSIS

Introduction

- 23. The options considered by the Panel are:

² Under the Takeovers (Fees) Regulations 2001, the Panel charges an application fee of \$100 (excl GST) and an hourly rate of \$145 (excl GST) for time spent by professional officers and employees in processing the application, and \$200 (excl GST) for time spent by Panel members.

- (a) retain the status quo; or
- (b) grant a class exemption from rule 6(1) of the Code for changes of trustees of family trusts.

Option 1: Retain Status Quo

24. Under this option, the Panel would continue to consider exemptions from rule 6(1) of the Code for changes of trustees on a case by case basis.

Analysis of Option 1

25. Option 1 would not alleviate the current cost/efficiency burden associated with processing individual exemptions. Rule 6(1) exemptions for trustees relate to relatively technical issues, but result in relatively high processing costs for family trusts. Accordingly, considering these types of exemptions on a case by case basis does not appear to maintain a proper relation between the costs of compliance with the Code and the benefits resulting from that compliance.
26. The Panel has taken a consistent approach to granting exemptions from rule 6(1) of the Code for trustees in these circumstances.
27. The Code is not intended to inhibit the re-organisation of family trusts that have no effect on the shareholders of a Code company.
28. For the reasons above, maintaining the status quo is not the preferred option.

Option 2: Grant a class exemption from rule 6(1) – preferred option

29. Under this option a class exemption would be granted from rule 6(1) of the Code for every person who:
- (a) becomes a trustee of a family trust, in respect of any increase in their holding or control of voting rights as a result of being appointed as a trustee to that family trust; or
 - (b) is a trustee of a family trust, in respect of any increase in their holding or controlling of voting rights as a result of a reduction in the number of trustees of that family trust.
30. The class exemption would be subject to conditions to the following effect:
- (a) the trustees are trustees of a private family trust established mainly to benefit:³
 - (i) relatives;⁴ or

³ Examples of the trusts in mind include the following (the list is not an exhaustive description):

- (a) Jill settles a trust for herself and her two children and any future spouses or partners and children. Jill and her mother are the trustees;
- (b) Trustees Pita and Kim and their lawyer establish a trust for the benefit of Pita's parents. None of the trustees is the settler nor a beneficiary of the trust.

⁴ Relative has the same meaning as in section 2 of the Securities Act 1978 which provides that "relative" has the same meaning as in the Tax Act 2007 (see Tax Act 2007 section YA1(c) set out at Appendix B).

- (ii) relatives of, or persons for whom, the settlor (or a person or persons with the power to appoint or remove trustees to or from the trust), has natural love and affection;
 - (b) under the trust deed the trustees must act unanimously;
 - (c) the appointment of a new trustee or reduction in the number of trustees is a bona fide reorganisation of the private family trust or is the result of an event beyond the control of the trustees, that does not have a collateral purpose of enabling a person to increase the person's holding or controlling of voting rights or the extent to which that person shares in the holding or controlling of voting rights in a Code company, otherwise than in compliance with the Code; and
 - (d) but for rule 6(2) of the Code, the reorganisation would not result in any increase in the percentage of voting rights in the Code company held or controlled by the trustees or the extent to which the trustees share in the holding or controlling of voting rights in the Code company.
31. The proposed conditions reflect the features that family trusts that have been the subject of exemption applications to the Panel have had in common, as set out in paragraph 18 above, except that the reference in paragraph 18(c)(i) to only the settlor having powers of appointment has been omitted from the proposed class exemption. This is because family trusts may not always involve the settlors. We raise the issue as to whether the proposed class exemption should include a condition regarding the settlor's or trustees powers of appointment in the Questions for Submissions that are set out on page 10.

Analysis of Preferred Option

32. Option 2 would provide certainty for this small area of the market. This is because family trustees, or persons wishing to become family trustees, who would be deemed by the Code to increase their control percentage under the circumstances that fall within the terms and conditions of the proposed exemption would have the certainty that the exemption is in place. They would not have to specifically seek an exemption from the Panel and nor in the circumstances where a trustee dies or must retire from the trust hurriedly, would the continuing trustees inadvertently breach the Code and then need to seek a retrospective exemption.
33. Option 2 would result in greater efficiency when compared with the status quo and would maintain a proper relation between the costs of compliance with the Code and the benefits resulting from such compliance. Persons seeking to rely on the class exemption would no longer have to make applications to the Panel. Trustees would avoid the burden of the current exemption process.
34. The conditions of the exemption should ensure that the class exemption applies only to the appointment of new trustees or a reduction in the number of trustees due to an event or bona fide reorganisation of the trust's affairs that does not have a collateral purpose of enabling a person to increase the person's voting control otherwise than in compliance with the Code. Therefore, there should be little possibility that there could be inappropriate reliance on the exemption.

35. The proposed class exemption relates to the bona fide reorganisation of family trusts that would have no effect on the shareholders of the Code company and in the Panel's view the Code is not intended to inhibit this type of reorganising of family trusts.
36. Option 2 could be implemented by the Panel quite quickly and a class exemption could take immediate effect. For the reasons above Option 2 is the Panel's preferred option.

CONCLUSION

37. The intended impact of the Panel's exemption role is the improvement in the functioning of the market by alleviating unintended or unreasonable consequences arising from the strict application of the Code.
38. It is timely to consider granting a class exemption from rule 6(1) of the Code for changes in trustees of family trusts resulting from either the appointment of new trustees to family trusts and/or the reduction in the number of trustees of family trusts.
39. The Panel has taken a consistent approach to reorganisations of family trusts in these circumstances, and has considered that the granting of a rule 6(1) exemption for trustees would be appropriate and consistent with the objectives of the Code.
40. The Panel is very concerned to get the right balance between enabling efficiency through granting of class exemptions and being a responsible market regulator.

QUESTIONS FOR SUBMISSIONS

41. The Panel seeks feedback on the options canvassed and welcomes any other proposals (and the reasons for those proposals) that market participants might have, specifically:

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| <ol style="list-style-type: none"> 1. Do you consider that the Panel has correctly identified the problem? If not, what is the problem in your view? 2. Do you agree with the Panel's policy objective? If not, what policy objective would you suggest instead? 3. Do you think that there is a risk of an inappropriate reliance on the proposed exemption? Please give reasons for your response. 4. Do you agree that the proposed exemption should be limited to changes in trustees of family trusts as outlined? If not, please give reasons for your response. 5. Do you consider that the conditions of exemption should require that there must be provisions in the trust deed relating to the settlor's powers of appointment and removal of trustees (or, where there is no settlor involved with the trust, the trustees' powers of appointment and removal of trustees)? If so, please give reasons for your response. 6. Do you agree with the suggested condition that, under the trust deed trustees must be required to act unanimously? If not, please give reasons for your response. 7. Do you agree with the other conditions of the proposed exemption? If not, can you suggest other conditions that would be more appropriate than those suggested by the Panel? |
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Appendix A

Rule 6(1) Exemptions for trustees

1. Takeovers Code (Vending Technologies Limited) Exemption Notice 2003
2. Takeovers Code (Pacific Print Group Limited) Exemption Notice 2005
3. Takeovers Code (Rakon Limited) Exemption Notice 2006
4. Takeovers Code (Speirs Group Limited) Exemption Notice 2006
5. Takeovers Code (Zintel Group Limited) Exemption Notice 2008
6. Takeovers Code (Westgate Power Centre Limited) Exemption Notice 2009
7. Takeovers Code (New Zealand Experience Limited) Exemption Notice 2009
8. Takeovers Code (Michael Hill International Limited) Exemption Notice 2009
9. Takeovers Code (Delegat's Group Limited) Exemption Notice 2010
10. Takeovers Code (Speirs Group Limited) Exemption Notice 2011

APPENDIX B

Income Tax Act 1978, section YA (1)(Definitions):

relative,—

(c) for the purposes of the definition of *relative* in section 2 of the Securities Act 1978, means a person connected with another person by—

- (i) being within the fourth degree of blood relationship to the other:
- (ii) being in a marriage, civil union, or de facto relationship with the other:
- (iii) being in a marriage, civil union, or de facto relationship with a person who is within the fourth degree of blood relationship to the other:
- (iv) being adopted as a child of the other or as a child of a person who is within the third degree of relationship to the other:
- (v) being the trustee of a trust under which a relative of the other person has benefited or is eligible to benefit.