In devising rules governing the conduct of takeover transactions, policy makers would serve the interests of investors and the economic order of society generally better by adopting regulations that maximise shareholder and social welfare. A mandatory bid rule can assist to achieve this objective. By significantly enhancing the chances of a takeover succeeding, that rule potentially encourages bidders to attempt more hostile acquisitions. An increase in search for potential takeover targets is likely to create some insecurity among directors and induce them to perform to their best level. Further, as takeovers facilitate the re-allocation of scarce societal resources to the parties to whom they have the highest valued uses, greater efficiency in the allocation of resources within industries is likely to be achieved as the incidence of hostile takeover transactions increases. Also, given that hostile takeovers are invariably made at a premium, an increase in that activity is likely to enhance shareholder wealth. These are matters of significant public importance. For this reason, it is advisable to reform the law governing takeover activity to introduce a mandatory bid rule in Australia.

Key terms Hostile takeovers; market for corporate control; takeover regulation; mandatory bid rule.

1 INTRODUCTION

In its discussion paper ‘Corporate Control: A Better Environment for Productive Investment’,¹ the Corporate Law Economic Reform Program² recommended the reform of

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the law governing takeover activity to introduce a mandatory bid rule in Australia. Under this proposal, a prospective acquirer would be allowed to cross the current 20% threshold and gain control of a company from some selected shareholders in private off-market transactions. This would be on the condition that the acquirer announced immediately an unconditional cash offer (or provide a cash alternative) for all the remaining voting shares in the company. Also, the offer would need to be made at the highest price paid over the preceding four months by the acquirer for shares in the target company. The stated objective of this recommendation was to promote a more vibrant market for corporate control and, ultimately, assist investors in public companies and society generally to more fully harness the positive effects of hostile takeover activity.

In making its recommendation, CLERP was guided by the view that hostile takeover activity confers substantial benefits upon shareholders and society generally. According to CLERP, the advantages of the hostile takeover process include acting as a mechanism for monitoring the performance of corporate management and facilitating the replacement of incompetent management teams. To this extent, hostile takeover activity serves to assure the quality of corporate management and, in the process, promotes productive efficiency. Indeed, the observation has been made by some commentators that ‘takeovers are . . . the critical corporate governance mechanism . . . without which managerial discretion cannot be

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2 Hereafter, this will be referred to by its acronym, CLERP.
4 CLERP, above, n 1 at 5.
5 Ibid, at 7.
6 Id.
effectively controlled.’ Further, CLERP recognised that hostile takeover activity has the potential to enhance the efficient allocation of resources within industries. It facilitates the re-allocation of scarce societal resources to the parties to whom they have the highest valued uses. An added advantage of hostile takeover transactions is that they invariably provide

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Quite significantly, the disciplinary and efficiency enhancing role of hostile takeovers have also been recognised by the corporations and securities regulatory authorities of various jurisdictions. See for example National Companies and Securities Commission, Discretions Vested in the Commission, Policy Release 105 [This policy statement is still applied by the Australian Securities and Investments Commission (ASIC). See ASIC, Practice Note 30 - NCSC Releases]; Canadian Securities Administrators, Take-over Bids - Defensive Tactics, Policy Statement No 38, (reproduced in CCH, Can Sec L Rep para 470-039) para 1; Department of Trade and Industry, Mergers Policy: A Department of Trade and Industry Paper on the Policy and Procedures of Merger Control, HMSO, London, 1988, para 2.27.

8 CLERP, above, n 1 at 8. This much has been recognised by several other commentators. See, by way of example, Bradley, above, n 7 at 367; Brudney, above, n 7 at 628; F H Easterbrook, & D R Fischel, ‘Corporate Control Transactions' (1982) 91 Yale Law Journal 698 at 705; J Pound & R J Zeckhauser ‘The Economics of Corporate Takeovers and the New Zealand Takeover Code: An Analysis and
offeree shareholders with an opportunity to earn a premium, thereby increasing aggregate shareholder wealth.\textsuperscript{9}

The CLERP recommendation was accepted by policy makers.\textsuperscript{10} Subsequently, to give it legislative effect, a proposed amendment to the \textit{Corporations Law} was passed by the House of Representatives.\textsuperscript{11} This initiative was, however, rejected by the Senate.\textsuperscript{12} The opposition


\textsuperscript{11} See \textit{Corporate Law Economic Reform Bill}, s 611, item 5. That provision, which was modelled on General Principle 10 and Rule 9 of \textit{The City Code on Takeovers and Mergers}, presently the principal regime of takeover regulation in the United Kingdom, relevantly provided:

\textit{Acquisition immediately followed by announcement of mandatory bid}

An acquisition that occurs in, or results from, the following circumstances:

(a) a person (the acquirer) acquires a relevant interest in securities of a body corporate: and

(b) those securities were held, immediately before the acquisition, by a particular person or by particular persons jointly (the prior holder or holders); and
was concerned that the proposed rule, if implemented, would not only disadvantage target shareholders\textsuperscript{13} but also generally emasculate the Eggleston principles upon which the present Australian regime of takeover regulation is based.\textsuperscript{14} 

This paper argues that in formulating rules governing the conduct of takeover transactions, policy makers would serve the interests of investors in public companies and the economic order of society generally better by adopting rules that maximise shareholder and social wealth.\textsuperscript{15} Proceeding from this premise, a plea is made for policy makers to reconsider the decision not to introduce a mandatory bid rule in Australia. Unlike some who believe that ‘the arguments against it clearly outweigh the arguments for it’\textsuperscript{16} the view taken here is that the benefits of a mandatory bid rule are likely to far outweigh its costs.\textsuperscript{17} Because of the substantial benefits that hostile takeover activity can bring to shareholders and the economy

\begin{itemize}
\item[(c)] the acquirer does not, at the same time as the acquisition referred to in paragraph (a), acquire a relevant interest in securities of the body held by someone other than the prior holder or holders; and
\item[(d)] immediately before the acquisition, the voting power of the acquirer in the body corporate is below 20%; and
\item[(e)] the acquisition is immediately followed by a public proposal by the acquirer, or an associate, to make an unconditional takeover bid for all the securities in the class to which the securities belong; and
\item[(f)] before the acquisition occurred, the prior holder or holders were informed that the acquisition would lead to that takeover bid.
\end{itemize}

The proposal under paragraph (e) must set out the terms on which the acquisition was made.

\textsuperscript{12} See the Commonwealth of Australia, Parliamentary Debates, \textit{Hansard}, Senate, AGPS, Canberra, 13 October 1999, at 9253 and 9650.

\textsuperscript{13} This issue is considered below in more detail. See Part 4 of this article.


\textsuperscript{15} On this see further L A Bebchuk, 'The Case for Facilitating Competing Tender Offers' (1981-82) 95 \textit{Harvard Law Review} 1028 at 1034.

\textsuperscript{16} See the Commonwealth of Australia, \textit{Hansard, above}, n 12 at 9650 (per Sen Conroy).

\textsuperscript{17} The potential benefits of a mandatory bid rule are explored in more detail in Part 3 of this article.
generally, the rules governing that activity should, from a shareholder and social welfare point of view, produce a large threat of hostile takeover transactions succeeding.\textsuperscript{18} A mandatory bid rule has the potential to achieve this objective. That rule increases the prospects of success of acquisition attempts. By so doing, it likely encourages prospective acquirers to undertake more search to identify potential takeover targets. Increased monitoring of corporate performance and the fear of displacement is likely to create some insecurity of tenure among directors and spur them to their best performance.\textsuperscript{19} This can only benefit shareholders. It likely makes current management more efficient. As well, the incidence of more hostile acquisitions is likely to ‘increase social welfare by moving productive assets to higher-valued uses and to the hands of better managers.’\textsuperscript{20}

The ensuing discussion is divided into six parts and is organised as follows. Part 2 outlines the legal procedures which, presently, must be observed by any person seeking to acquire control of a public company. That part goes on to argue that the rules now in force are a potential disincentive to hostile takeover activity and that by discouraging that activity, current law potentially imposes substantial costs on investors and society in general. Part 3 demonstrates that many of the difficulties engendered by current takeover law can be overcome through the implementation of a mandatory bid rule. Part 4 examines and attempts to rebut some of the arguments commonly advanced against the mandatory bid rule, thus laying the foundation for the resurrection of the proposal to introduce that rule in Australia. Part 5 explores ways in which the law could be reformed to introduce a workable mandatory bid rule. Some conclusions follow in Part 6.


\textsuperscript{20} \textit{Ibid, at} 1182.
2 CURRENT LAW

Presently, the Corporations Act 2001 (Cth) prohibits any person,\(^{21}\) subject to some exceptions,\(^{22}\) from acquiring between 20 and 90 percent of the voting shares of a company unless an offer is made to all shareholders of the relevant class of shares to be acquired.\(^ {23}\) The aim of these restrictions is to ensure that a person does not acquire too great an interest in a company unless some exemption applies or Chapter 6 of the Corporations Act has otherwise been complied with.\(^ {24}\) The threshold is set at 20% because it is believed that at this level, control of a company is likely to change.\(^ {25}\) Effectively then, control of a company can pass only after a formal takeover offer has been made. ‘Pre-bid agreements or understandings between bidders and target shareholders are prohibited, where they would operate to take the bidder over the statutory threshold.’\(^ {26}\)

Prior to making its offer, a prospective acquirer is required to prepare a statement containing certain prescribed information (the Bidder’s Statement). That statement, together with a copy of the bidder’s pro-forma offer, must then be lodged with ASIC.\(^ {27}\) Further, the bidder is subject to a pre-offer notification requirement. It must serve a copy of its Bidder’s Statement upon the target company 14-28 days before dispatching its offer to the offeree shareholders.\(^ {28}\) Finally, an offer, once made, must be kept open for acceptance for at least one month.\(^ {29}\)

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\(^{21}\) See Corporations Act 2001 (Cth), s 606(1).

\(^{22}\) As to these, see Corporations Act 2001 (Cth), s 611.

\(^{23}\) See Corporations Act 2001 (Cth), s633(1) Item 6.

\(^{24}\) Afro-West Mining Ltd v Australian Mining Investments Ltd (1989) 7 ACLC 618 at 623 (Supreme Court of New South Wales – per Cohen J). See further Little, above, n 9 at 45.


\(^{26}\) CLERP, above, n 1 at 19.

\(^{27}\) Corporations Act 2001 (Cth), 633 Items 1 and 2.

\(^{28}\) Corporations Act 2001 (Cth), 633 Item 3.

\(^{29}\) Corporations Act 2001 (Cth), s624(1)(b).
These rules are based on the recommendations of the Company Law Advisory Committee which was established in 1969 by the Standing Committee of State and Commonwealth Attorneys-General of Australia to study and make recommendations on the administration of companies and securities laws. They seek to improve the protection of the interests of shareholders by ensuring, among other things, that control of publicly listed companies does not pass by stealth or discriminatory arrangements. They also aim to assure every shareholder an opportunity to participate in any benefits payable on a change of corporate control. A further objective of the rules is to ensure that all offeree shareholders have adequate time to receive an offer and study its merits.

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30 This committee is popularly referred to as the Eggleston Committee, after its chairman Sir Richard Eggleston. The committee recommended the introduction of legislative measures to regulate the conduct of takeover transactions. The Committee further recommended that the object of such measures should be neither to encourage nor discourage takeover activity but to ensure that:

(a) the shareholders and directors of a company know the identity of the person who proposes to acquire a substantial interest in the company;

(b) the shareholders and directors of a company have a reasonable time in which to consider any proposal under which a person would acquire a substantial interest in the company;

(c) the shareholders and directors of a company are supplied with sufficient information to enable them to assess the merits of any proposal under which any person would acquire a substantial interest in the company;

(d) as far as practicable, all shareholders of a company have equal opportunities to participate in any benefits accruing under any proposal under which a person would acquire a substantial interest in the company.

These principles (popularly referred to as the Eggleston criteria) are now enshrined in the legislation as matters which must be observed by all participants in the takeover process - see Corporations Act 2001 (Cth), s602.

For the Committee’s full recommendations concerning the regulation of takeover activity see Disclosure of Substantial Shareholdings and Takeovers (The Second Interim Report), Parliamentary Paper No 43/69.


Whilst serving these lofty objectives, the current regulatory regime unnecessarily hinders the smooth operation of a competitive market for corporate control, as the discussion in the next Part will endeavour to show. This is undesirable. By erecting unnecessary barriers in the way of potential acquirers, current law potentially deters some otherwise beneficial changes in corporate control. This is likely to frustrate the disciplinary, allocative and wealth maximising roles of the hostile takeover process. In consequence, shareholder and social welfare are bound to be harmed.

2.1 The costs of current law

2.1.1 Current law promotes free riding

It will be apparent from the foregoing exposition that, presently, the Corporations Act delays the conclusion of hostile takeover transactions for significant amounts of time. Such extended delay is detrimental to the interests of acquirers. Bidders can protect and, consequently, appropriate fuller value from their investment in information only if a takeover is conducted and concluded with reasonable despatch. By preventing prospective acquirers from concluding hostile takeover transactions as quickly as they can, current law destroys the element of speed. At the same time, it augments the chances of premature leakage of commercially sensitive information. Such an eventuality not only attenuates the searcher’s property rights in information, it also renders attempting acquisitions quite risky. The registration of the bidder’s statement, pre-offer notification and the making of a takeover offer tip off the market. The extended delay involved in these processes gives rivals, who

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may not have incurred search costs, an opportunity to enter the contest\textsuperscript{34} and possibly outbid the initial offeror.\textsuperscript{35} The emergence of competing bids leads to a greater likelihood of the initial bidder being frustrated in its intentions. This factor is likely to reduce the incentive on the part of many prospective acquirers to engage in search and be the first bidder.\textsuperscript{36} As prospective acquirers desist from engaging in search, there is likely to follow less than optimum monitoring, leading to a potential decrease in the efficiency of corporate management.\textsuperscript{37} In the result, shareholder and social welfare are certain to be diminished.

2.1.2 Current law raises the cost of takeovers.

More seriously, by facilitating the entry of rival bidders, current law potentially raises the financial cost of takeovers. Indeed, this issue was eloquently highlighted by CLERP when it observed that:\textsuperscript{38}

\begin{quote}
by generally precluding control from changing hands other than during a bid, the takeover provisions facilitate auctions for corporate control. In particular, the provisions requiring . . . minimum offer periods and a minimum period between the announcement and opening of an offer make it possible for other parties to contest the bid by offering a higher price.
\end{quote}

It is maintained by some that the auction process enhances shareholder welfare and so should be fostered. Adherents of this view point out that competing bids operate as a cost free bargaining mechanism for offeree shareholders, enabling them to earn a higher premium

\begin{thebibliography}{99}

\bibitem{34} See generally Little, \textit{above}, n 9 at 45. For an interesting discussion of the free-rider problem generally, see S Levmore, ‘Monitors and Freeriders in Commercial and Corporate Settings’ (1982) 92 \textit{Yale Law Review} 49.

\bibitem{35} The problem of competing bids is treated in more detail in Part 4.1 below.


\bibitem{37} Winsen, \textit{above}, n 7 at 103.

\bibitem{38} CLERP, \textit{above}, n 1 at 15 and 20.
\end{thebibliography}
without incurring any bargaining costs. Indeed, this argument has been used with telling effect by some parties opposed to changing the present regulatory regime. For example, in his speech during the Senate debate on the mandatory bid rule, Senator Conroy said:

The opposition understands the arguments for the mandatory bid proposal . . . But it comes at a cost that is more than the opposition is willing to risk. . . . No longer will there be an appropriate competitive regime for corporate control and, despite the proposed safeguards, shareholders will not get a better price than that obtained from an auction process.

Although an auction might benefit offeree shareholders in the short term, it is likely to work counter to their long term interests. We learn from economic theory that an increase in price is likely to cause demand for a commodity to fall. By significantly raising the financial cost of acquiring control, auctions reduce the profitability of corporate control transactions. Eroding the potential profits of prospective bidders is likely to reduce the incentive to attempt acquisitions. As Grossman and Hart have rightly observed, ‘no raid will take place if a bidder is to pay at least as much for the firm’s shares as they are worth to him.’ The prospect of a bidding war is thus likely to dampen the enthusiasm of many prospective bidders. It is an observed fact that ‘some persons are reluctant to commit the necessary time, effort and expense to make a bid if they believe that it will be used as a “stalking horse”’

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41 Commonwealth of Australia, Hansard, above, n 12, at 9650.


43 See generally Little, above, n 9 at 45; Grossman & Hart, above, n 18 at 45.

44 Gutman, above, n 31 at 632.
to obtain higher bids.\textsuperscript{45} If initial bids are not forthcoming, shareholders whom the law seeks to protect will, instead, lose out. Social welfare will also likely be diminished.

### 2.1.3 Current law facilitates resistance by incumbent directors.

Apart from facilitating the entry of rival bidders into the contest, extended delay also gives target management an opportunity to organise and set in place defensive mechanisms to thwart any takeover offer unacceptable to them.\textsuperscript{46} The spectre of resistance increases the risks of the bidder’s intentions ultimately being frustrated by incumbent management. Indeed, based on the findings of studies conducted by himself and others, Eddey has asserted that ‘if target directors . . . actively defend against a bid, then the probability of the bid being successful is low.’\textsuperscript{47} In fact, there are innumerable instances in Australia where incumbent directors have successfully resisted unsolicited takeover overtures. The fear of being frustrated, perhaps for irrelevant considerations, is likely to chill the incentive of some prospective acquirers to engage in search or be the first bidder.\textsuperscript{48}

It thus appears that the results of the current regulatory regime are most unfortunate. By promoting prolonged delay, it introduces uncertainty into takeover transactions, thereby rendering acquisition attempts more risky than they need be. Further, it raises the cost and,


\textsuperscript{46} This matter is discussed in more detail in Part 4.5 below.

\textsuperscript{47} P H Eddey, ‘Corporate Raiders and Takeover Targets’ (1991) 18 Journal of Business Finance & Accounting 151 at 164-5. See also Little, above, n 9 at 526.

\textsuperscript{48} On this see further M Roe, Strong Managers, Weak Owners - The Political Roots of American Corporate Finance, Princeton University Press, Princeton, New Jersey, 1994 at 152; Winsen, above, n 7 at 94.
consequently, reduces the profitability of hostile takeover transactions. These factors are likely to operate as significant disincentives to takeover activity. Given the important role that the hostile takeover process plays in promoting shareholder and social welfare, it is desirable to reform the current regulatory regime to minimise its undesirable effects. Otherwise, potential bidders may be constrained to resort to alternative acquisition methods. Indeed, there is some evidence of this already happening. In the recent past, there has been a noticeable increase in the use of schemes of arrangement to effect acquisitions of corporate control. There is a distinct possibility that this can be attributed to the difficulties engendered by the current takeover procedure.\footnote{On the use of the scheme of arrangement as an alternative acquisition strategy see H A J Ford et al, \textit{Ford's Principles of Corporations Law}, 11th ed 2003, Lexisnexis Butterworths, Sydney, para 24.020 (at 1100-01) and para 24.060 (at 1107-8); A Colla, ‘Schemes of Arrangement as an Alternative to Friendly Takeover Schemes: Recent Developments’ (1998) \textit{16 C & SLJ} 365 especially at 379-380.} If this trend persists, shareholders and society generally will increasingly be denied the benefits of takeover activity.\footnote{On this see further ‘Arranged Marriage: Are Schemes of Arrangement Being Used to Bring Parties Together Against Their Will? [2003] \textit{Australian Corporate News} 173. This Note documents a case where a scheme of arrangement was recently used to acquire a company despite the strong opposition of many shareholders over the offer price. Here, HBOS, a 57% shareholder in BankWest, bid $4.25 a share to acquire the bank’s remaining shares. The offer price was only slightly higher than the stock’s market price, which was then hovering around $4.20 per share. The transaction succeeded, despite the misgivings of many shareholders who variously described the offer price as ‘parsimonious’ and ‘stingy’ (see [2003] \textit{Australian Corporate News} 173 at 174). It is probable that if the acquisition had proceeded by way of a takeover offer, shareholders would have been able to earn a more substantial premium. Whilst there is no general agreement on this point, it is generally believed that a premium of at least 25% must be offered for any takeover offer to stand a chance of success - see for example Bishop \textit{et al, above}, n 7, at 26; Lonergan, \textit{above}, n 9 at 338.}

3 IMPROVING THE LAW: THE PROMISE OF THE MANDATORY BID RULE

If introduced, a mandatory bid rule, such as that proposed by CLERP, can significantly improve the operation of the market for corporate control in Australia. This is likely to benefit of both investors in Australian companies and society generally. The following discussion seeks to demonstrate this.
3.1 The rule promotes speed in the conclusion of hostile takeover transactions.

A mandatory bid rule, of the nature recommended by CLERP, enables acquirers to conclude hostile takeover transactions with speed and in privacy, as desired. To this extent, the rule assists to overcome most of the risks discussed before. Most significantly, it assures bidders of success. By improving the chances of success of hostile acquisitions, the rule is likely to encourage prospective acquirers to undertake more search for takeover targets. An increase in the level of search is, in turn, likely to create a degree certain of fear among corporate management and induce them to perform with greater efficiency. The rule is thus likely to serve as ‘an engine of corporate accountability.’ As Professor Coffee Jr has observed:

> the constant search for . . . discounted bargains both motivates the managements of marginal firms towards increasing performance lest they become targets, and deters conduct injurious to shareholders – all without the need for regulatory intervention.

To the extent that this is achieved, shareholder and social welfare will likely be enhanced.

3.2 The rule encourages the assembly of strategic control blocs.

If implemented, the proposed mandatory bid rule would remove the prohibition against the acquisition of corporate control in private, off-market transactions presently in force. This can benefit shareholders in a very important respect. It is likely to encourage the assembly of strategic control blocs and consequently assist in reducing the agency costs of management.

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51 See generally the discussion in the preceding part of this article.
52 See further Colla, above, n 49 at 379-380.
53 See discussion accompanying note 18 above.
55 Ibid, at 1155.
It is well known that one of the quintessential characteristics of the modern large company is dispersed shareholders with small holdings and concentrated management. With fragmented shareholders typically owning only small holdings, no individual shareholder has a large enough incentive to devote resources to ensuring that management are acting in the interest of the shareholders. This has the potential to make directors less accountable in a way that can hurt shareholders. Indeed, in their seminal work, *The Modern Corporation And Private Property*, published in 1932, Berle and Means asserted that the direct consequence of the ownership structure of modern large firms was to release management from the overriding requirement that it serve its stockholders. They further opined that:

> the concentration of economic power separate from ownership has, in fact, created economic empires, and has delivered these empires into the hands of a new despotism, relegating the new owners to the position of those who supply the means whereby the new princes may exercise their power.

By facilitating the emergence of holders of control blocs (perhaps where there was none before) the mandatory bid rule can assist to overcome the collective action problems that

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make small shareholders passive. Large bloc owners have both the incentive and ability to monitor management performance. Because of this, they can influence corporate management and reduce the agency costs of corporate governance. Out of self-interest, large shareholders keep a watchful eye open in order to safeguard their interest. This provides an incentive to management to adopt policies in the interest of shareholders. True, large investors do not normally interfere with purely managerial decisions. Ordinarily, they follow the Wall Street Rule. They simply liquidate their holdings if dissatisfied with management performance. All the same, as Pennington rightly observed, 'institutional investors are known to have certain predilections on general issues which directors are careful not to flout.' Management are only too aware that if large investors disapprove of their conduct of a company's affairs, they will express their dissatisfaction by selling their holdings, which might result in management losing their positions and perquisites. This is likely to inspire management to improve their performance.

By encouraging the assembly of control blocs, the mandatory bid rule likely provides a better monitor of incumbent management. This benefits the company and all shareholders.


Bhagat et al, above, n 62 at 13. See also Berglof & Burkart, above, n 7 at 191; Hill, above, n 62 at 597; Mannolini, above, n 3 at 213.

Roe, above, n 48 at XIV.

This phenomenon is evidently still prevalent in Australia today, as recent findings on the voting trends of the largest shareholders in Australian companies indicate. See, for example, Mannolini, above, n 3 at 197; Stapledon, above, n 58 at 253; F Buffini, ‘Institutions Still Loath to Use Voting Power’ The Australian Financial Review, 11 March 2004, at 5.

Easterbrook & Fischel, above, n 19 at 1171; Andre, above, n 39 at 867; Stapledon, above, n 58 at 128 and 257.


Coffee Jr, above, n 54, at 1284.
process of monitoring by large shareholders poses a continuous threat of takeover if performance lags. In order to reduce the chances of takeover, managers will endeavour to pursue policies that favour the company, leading to a reduction in agency costs.\(^69\) Indeed, it has been argued that the value of a firm increases when an investor takes a large-block position.\(^70\)

Further, in addition to promoting enhanced monitoring of management performance, the assembly of control blocs is likely to raise the probability of success of value-enhancing takeovers. It has been postulated that where shares in a company the subject of a takeover bid are widely held, small shareholders have no incentive to tender their shares. These shareholders, believing that the bid will succeed without their participation, are likely to hold on to their shares, hoping to benefit from a change in management, in the expectation that sufficient other shareholders will accept the offer.\(^71\) This phenomenon has the potential to lead to the frustration of a takeover bid through non-acceptance. On the other hand, holders of control blocs do recognise that without their participation, a bid may fail. They thus have an incentive to seek out and accept value-enhancing bids.\(^72\) The existence of holders of strategic control blocs is thus likely to facilitate more takeovers relative to a company with dispersed shareholders.\(^73\)

\(^{69}\) Easterbrook & Fischel, above, n 19 at 1174.

\(^{70}\) Bhagat et al, above, n 62 at 8 (citing Mikkelsen and Rubac); Ayres & Cramton, above, n 58 at 1049 (citing Shleifer and Vishny).

\(^{71}\) See generally Grossman & Hart, above, n 18 at 44-7.

\(^{72}\) Id. See also Ayres & Cramton, above, n 58 at 1042-3.

\(^{73}\) Id. See also Berglof & Burkart, above, n 7 at 185.
3.3 The rule assists to reduce the financial cost of takeovers.

In a very erudite article published in the influential Columbia Law Review, Professor Coffee Jr counselled that: 74

the more the law can reduce the tender offer premium necessary to secure working control of the target corporation, the easier and more frequent hostile takeovers will become, thereby reducing agency costs and increasing shareholder wealth.

A mandatory bid rule can play a crucial role in attaining the objective checking the level of premium payable upon a transfer of corporate control. That rule enables an offeror to acquire control of a company before other bidders have had time to advance a competing bid. The auction process is effectively eliminated. 75 By enabling bidders to retain more of the gains from takeover transactions, the rule is likely to provide more incentives to bidders to attempt acquisitions.

4 OPPOSITION TO THE MANDATORY BID RULE

Whilst it appears that a mandatory bid rule could significantly improve the functioning of the market for corporate, to the benefit of shareholders and society in general, there is some anxiety in certain influential quarters that it could also harm the interests of investors in Australian companies. As a result, the introduction of the rule has, at least for the time being, been deferred. It is thus important to evaluate and rebut the criticisms levelled at the rule. That forms the task of this Part.

4.1 The rule is likely to lead to a reduction in shareholder wealth.

74 Coffee Jr, above, n 54, at 1154.
75 As to why this is desirable, see the discussion in Part 4.1 below.
The opinion has been expressed that ‘an efficient mechanism for discovering the highest price that a buyer will pay for a controlling stake in a target company requires informed competition between prospective buyers.’\textsuperscript{76} However, a mandatory bid rule has potential to deny shareholders the benefit of an auction for their shares. As CLERP forthrightly recognised in its discussion paper:\textsuperscript{77}

under a mandatory bid, control could pass prior to the making of a formal takeover bid. This would preclude rival bids and the opportunity for an auction for control. An auction facilitates price competition in the market by compelling a bidder to pay an amount at least as high as others are, or might be, willing to pay. In the absence of this competition, it is argued that bidders may acquire targets for a lower premium, harming the interests of target shareholders by depriving them of the ‘true’ value of their shares.

Because it is likely to prevent shareholders from receiving the highest possible price for their shares, it is considered by some that a mandatory bid rule is undesirable. It potentially diminishes shareholder wealth.\textsuperscript{78} Indeed, this is one of the most powerful arguments commonly advanced in opposition to its introduction.\textsuperscript{79} To these critics, no acquisition should occur before other bidders have had time to advance a competing bid. That way, takeover offer premiums will be maximised.\textsuperscript{80}


\textsuperscript{77} CLERP, \textit{above}, n 1 at 21 (notes omitted).

\textsuperscript{78} See, for example, Bebchuk, \textit{above}, n 14 especially at 1038-41.

\textsuperscript{79} See for example the Commonwealth of Australia, \textit{Hansard, above}, n 12 at 9650-1 (per Sen Conroy) and at 9652 (per Sen Murray); Philips, \textit{above}, n 76; Levy & Patrick, \textit{above}, n 3 at 424; B Frith, ‘Fix the Bidding or Bin it Again’ \textit{The Australian}, 4 April 2003 at 18.

\textsuperscript{80} Andre, \textit{above}, n 39 at 906; Bebchuk, \textit{above}, n 14 at 1038.
It is acknowledged that ‘to the extent that auctions raise the takeover premium, they obviously reduce the possibility of exploitation of the target’s shareholders.’\textsuperscript{81} From this point view, ‘ex post competition will always be desirable.’\textsuperscript{82} However, as already argued, from a social welfare point of view, the law should endeavour to increase the chances of takeovers occurring as this makes current management very efficient.\textsuperscript{83} This is likely to happen if the cost of acquiring control of a company is lower than its expected value to the bidder.\textsuperscript{84} It thus appears that measures which promote auctions are not necessarily desirable. By driving up the offer premium that must be paid for corporate control, competitive bids may discourage raids from ever taking place.\textsuperscript{85} It is well known that ‘demand curves almost invariably slope down to the right.’\textsuperscript{86} Thus, it is evident that any increase in the expected cost of acquiring control is certain to ‘generally discourage prospective bidders for others targets; when the price of anything goes up, the quantity demanded falls.’\textsuperscript{87} Fewer hostile takeover offers will be made. So, if the law insists on achieving very high takeover premia, the result is likely to be a sacrifice in the level of takeover activity, leading to reduced managerial efficiency.\textsuperscript{88} Indeed, this much has been recognised by the City Panel on Takeovers and Mergers, the principal regulator of takeover activity in the United Kingdom. Its Code does not seek to promote competitive bidding. Explaining the reason for this approach, Sir Alexander Johnston, a former Deputy Chair of the Panel said:\textsuperscript{89}

\begin{itemize}
\item \textsuperscript{81} Coffee Jr, \textit{above}, n 54 at 1174.
\item \textsuperscript{82} Grossman & Hart, \textit{above}, n 18 at 58.
\item \textsuperscript{83} \textit{Ibid}, at 60.
\item \textsuperscript{84} \textit{Ibid}, at 46.
\item \textsuperscript{85} Coffee Jr, \textit{above}, n 54 at 1176; Grossman Hart, \textit{above}, n 18 at 58.
\item \textsuperscript{86} Coffee Jr, \textit{above}, n 54 at 1176; Mankiw, \textit{above}, n 42 at 76-9.
\item \textsuperscript{87} See generally the works cited in note 42 above; Easterbrook & Fischel, \textit{above}, n 19 at 1176; Coffee Jr, \textit{above}, n 54 at 1176; Mannolini, \textit{above}, n 3 at 203-4.
\item \textsuperscript{88} On this, see further Grossman & Hart, \textit{above}, n 18 at 53; Mannolini, \textit{above}, n 3 at 204.
\item \textsuperscript{89} Sir Alexander Johnston, \textit{The City Take-Over Code}, Oxford University Press, 1980 at 104.
\end{itemize}
if the code insisted on what might seem to be a public auction of the company, a potential offeror willing to offer good terms might find this prospect unattractive and go away: and then all concerned would be losers.

Apart from raising the financial cost of acquiring corporate control, auctions are undesirable for another important consideration. It has been observed that the first bidder generally loses in a competitive bidding contest. Indeed available studies indicate that the initial bidder loses in 75% of the cases when a second bid is made. It has also been established that when a corporate bidder loses a control contest and the target is instead captured by a rival firm the losing bidder’s stock declines significantly. Truly, ‘to a management concerned with maximizing its firm’s stock value, this is a substantial disincentive. . . Not only are the odds high that it will fail to obtain control but there is strong empirical evidence that its own share value will fall in the wake of its defeat in a control contest over the target. This is likely to operate as a potent disincentive for a prospective acquirer to initiate a control contest. As Professor Winsen warned sometime back, ‘if in an auction market the second bidder consistently wins, there may be inadequate incentives for the first bidder to make the initial offer that starts the contest, hence the auction market might collapse.’ This does not augur well for shareholders.

Further, in considering whether auctions are good for shareholders, it is essential to take account of the fact that quite often competing bidders are able to offer more than the initial offeror because they may not have incurred search costs. In any event, it has been observed that the price paid by competing offerors is often only slightly higher than that offered by the

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90 Coffee Jr, above, n 54 at 1289.
91 Ibid, at 1178.
92 Id.
94 Coffee Jr, above, n 54, at 1281.
original bidder.\textsuperscript{95} Thus, the gains from competing offers may not be very large. However, the loss sustained when initial bids are discouraged may be substantial.\textsuperscript{96} In this connection, \textit{Darvall v North Sydney Brick & Tile Company Limited (No 2)} provides an excellent illustration.\textsuperscript{97}

In this case, a cash takeover offer of $10 per share was made for all the outstanding shares in the respondent company. The last recorded trading price of those shares prior to this offer was 0.87 cents. Thus, as Kirby P (as he then was) observed, the offer represented ‘a tenfold increase in the value of the shares over their last sale’.\textsuperscript{98} The directors of the target company promoted a competing offer claiming, among other things, that they wished to secure a higher price for the shareholders.\textsuperscript{99} This led to the frustration of the original offer. However, the competing offer was made at $11 per share, representing a gain of a mere 10% over the original offer.\textsuperscript{100} It is not difficult to see that this scenario is likely to discourage initial bids, to the disadvantage of shareholders.

It is thus imperative to ensure that in the endeavour to secure high takeover prices, the law does not stymie desirable takeover activity. This could limit the disciplinary and resource allocation roles of hostile takeover bids,\textsuperscript{101} and a consequent reduction in shareholder and social welfare. Therefore, it is important to resist the allure of competing bids. Very clearly, as Professors Easterbrook and Fischel argued in their penetrating analysis of the utility of

\begin{footnotesize}
\begin{tabular}{ll}
\textsuperscript{95} & Winsen, \textit{above}, n 7 at 95 (quoting Grossman & Hart). \\
\textsuperscript{96} & \textit{Ibid}, at 95-6. \\
\textsuperscript{97} & (1989) 7 ACLC 659 (NSW Court of Appeal). \\
\textsuperscript{98} & \textit{Ibid}, at 665. \\
\textsuperscript{99} & See generally \textit{Ibid}, at 702-4. \\
\textsuperscript{101} & Grossman & Hart, \textit{above}, n 18 at 53. \\
\end{tabular}
\end{footnotesize}
competitive bidding ‘any approach that looks only at the way in which managers can augment the tender offeror’s bid given that a tender offer has already been made, but disregards the effect of a . . . strategy on the number of offers that will be made in the future and the way in which the number of offers affect the efficiency with which corporations are managed, ignores much that is relevant to shareholders’ welfare.’

Finally, it is significant to note that it has been observed in the United Kingdom that even without auctions, there is no evidence that the best price is not obtained in corporate control transactions. There is nothing to suggest that the conditions prevailing in Australia are radically different from those obtaining in the United Kingdom. This makes the argument that it is essential to have competitive bidding as a means of ensuring that shareholders secure the highest possible price that much weaker.

4.2 The rule will disadvantage shareholders where the selling controlling shareholder is in a distressed state.

While still on the question of price, critics of the mandatory bid rule have further argued that in the absence of competing bids, the price available to shareholders may not be maximised in cases of distressed sales.

This criticism can be disposed of easily. Under the proposed rule, following the acquisition of a controlling interest, an offer would need to be made to the remaining shareholders not at the price paid to the owner or owners of the control parcels, but at the highest price paid over

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102 Easterbrook & Fischel, above, n 19 at 1164.
104 See the Commonwealth of Australia, Hansard, above, n 12 at 9651 (per Sen Conroy); Mannolini, above, n 3 at 212; Levy & Patrick, above, n 3 at 426; R Levy, ‘Pre-Bid Stake Building’ (2001) 19 C&SLJ 205.
the preceding four months by the acquirer for shares in the target company.\textsuperscript{105} This should dispel the concern that remaining shareholders will necessarily be disadvantaged if the selling controlling shareholder’s main objective is not to obtain the best possible price. The rule contains within it a mechanism – the highest price principle - to ensure that minority shareholders receive an equitable price. In any event, it is important not to forget, in the words of Grossmann and Hart that ‘there is a real trade off between achieving a high tender price and inducing managerial efficiency, shareholders pursuit of the former leads to a (partial) sacrifice of the latter.’\textsuperscript{106} Indeed, it has been asserted that ‘to foster efficiency, a takeover mechanism must grant to bidders benefits that do not accrue to other shareholders on a pro-rata basis.’\textsuperscript{107} If the mandatory bid rule assists to lower the price payable on a transfer of corporate control, and thereby induces more takeover activity, leading to improved managerial performance, so much the better. As Hertig and McCahery have advised, one of the objectives of policy makers should be to promote policies that make takeovers less costly and thus produce more bids.\textsuperscript{108}

4.3 The rule is likely to diminish allocative efficiency.

Apart from the shareholder welfare concerns discussed above, proponents of the competitive auction process also seek to discredit the mandatory bid rule on grounds of social welfare. The argument is put that the auction process helps to ensure that the target is acquired by the

\textsuperscript{105} See Corporate Law Economic Reform Bill, s 611, item 5.

\textsuperscript{106} Grossman & Hart, \textit{above}, n 18 at 53.

\textsuperscript{107} Berglof & Burkart, \textit{above}, n 7 at 182.

firm that values it the most.\textsuperscript{109} This ostensibly benefits society by ensuring that the target's assets are shifted their most productive uses, thereby promoting allocation efficiency.\textsuperscript{110}

This argument is certainly respectabe. There can be no doubt that the interest of society lies in scarce societal resources being put to their highest valued uses. However, this argument fails to appreciate that quite often, competing offers come about because someone is taking a free ride on information generated by the first bidder. As argued before, free riding of this sort is undesirable.\textsuperscript{111} It reduces the incentive to undertake search and make the first offer. In the long run, the amount of monitoring is reduced and the number of offers decreases. This is likely to harm, rather than promote, shareholder and social welfare.\textsuperscript{112}

4.4 The rule is likely to extinguish the role of directors in contests for corporate control.

Chapter 6 of the \textit{Corporations Act}, which regulates takeover activity, has as its objective to ensure, among other things, that:\textsuperscript{113}

\begin{enumerate}
  \item the shareholders and directors of a company know the identity of the person who proposes to acquire a substantial interest in the company;
  \item the shareholders and directors of a company have a reasonable time in which to consider any proposal under which a person would acquire a substantial interest in the company;
\end{enumerate}

\textsuperscript{109} See for example Andre, \textit{above}, n 39 at 906.
\textsuperscript{110} Gilson, \textit{above}, n 36 at 62; Bebchuk, \textit{above}, n 14 at 1048-1050; Coffee Jr, \textit{above}, n 54 at 1145 and 1280 et seq.
\textsuperscript{111} See discussion in Part 2.1.2 above.
\textsuperscript{112} Easterbrook & Fischel, \textit{above}, n 19 at 1189.
\textsuperscript{113} See \textit{Corporations Act (Cth)} 2001, s602(b).
However, if implemented, the proposed mandatory bid rule would change this position and, instead, make it possible for a bidder to acquire control of a company without first declaring its intentions to the directors of the target company.\textsuperscript{114} For this reason, the proposal has also been roundly criticised. In particular, it has been said that the rule would work contrary to the interests of minority shareholders to the extent it would deny them the benefit of their directors’ advice in transactions involving the transfer of control of their company.\textsuperscript{115} Indeed, commenting on this particular aspect of the rule, Senator Conroy said:\textsuperscript{116}

\begin{quote}
    The mandatory bid rule . . . would go against the Eggleston principles . . . It is important to reiterate what those Eggleston principles are. . . The Eggleston principles require: that shareholders of a target takeover company know the identity of any person that proposes to acquire a substantial interest in the company; that target shareholders and directors have sufficient time to consider the offer; . . . The mandatory bid rule breaks these principles.
\end{quote}

With respect, the involvement of the directors of the target company in the takeover process is not desirable.\textsuperscript{117} A hostile takeover offer presents target directors with a potential conflict of interest.\textsuperscript{118} ‘Managers of the target perceive bids as reflecting poorly on their services,
since the bidder proposes to change the way the target is run.\textsuperscript{119} Further, with the success of a hostile takeover offer, the incumbent directors often stand to lose their positions and perquisites. Faced with a hostile takeover bid then, ‘there is a great danger that the directors will channel their expertise toward pursuit of personal advantage,’\textsuperscript{120} in conflict with their duty to act in best interests of the company.\textsuperscript{121} By allowing target directors a role in determining the outcome of a hostile takeover offer,\textsuperscript{122} current law significantly weakens the protection of the interests of the company and its shareholders. The directors are given sufficient scope to take action to block a transfer of control unacceptable to them. Current law thus potentially serves as an instrument of directorial entrenchment and works contrary to the objective of promoting accountability and efficiency. Since ‘there is no signal that separates intransigent resistance from honest efforts to act for the shareholder’s benefit,’\textsuperscript{123} the directors can resolve to resist a takeover attempt in furtherance of their own parochial interests. The directors ‘may try to resist - whether crassly to save their jobs or because they genuinely believe that their program is superior to the bidder’s.’\textsuperscript{124} Or they may act so as to facilitate the company to be acquired by a bidder that promises not oust them from their


\textsuperscript{120} \textit{Johnson v Trueblood} 629 F 2d 287 at 300 (per Rosenn J). See also Little, \textit{above}, n 9 at 525; R J Gilson, ‘Unocal Fifteen Year Later (and What We Can Do About It)’ \textit{Delaware Journal of Corporate Law}, Vol. 26, No. 2, pp. 491-513 \url{http://ssrn.com/abstract=333041} (date accessed 23 April 2004) at 495.


\textsuperscript{122} As presently interpreted, the fiduciary standard, which governs the duties of directors in takeover situations, gives target management wide scope to adopt measures to repel any unsolicited takeover bid. As to this, see generally \textit{The Australian Metropolitan Life Assurance Company Limited v Ure} (1923) 33 CLR 199; \textit{Harlowe’s Nominees Pty Ltd v Woodside (Lakes Entrance) Oil NL} (1968-69) 42 ALJR 123; \textit{Darvall v North Sydney Brick & Tile Company Limited (No 2)} (1989) 7 ACLC 659.

\textsuperscript{123} Easterbrook & Fischel, \textit{above}, n 19 at 1178.

\textsuperscript{124} Easterbrook & Fischel, \textit{above} n 119 at 162. See also Berglof & Burkart, \textit{above}, n 7 at 195.
positions after the merger, or to confer on them extra side benefits, rather than one offering the best terms.\textsuperscript{125}

The proposed mandatory bid rule goes a long way in overcoming these difficulties. It effectively ensures that target directors, who may be ineffective, cannot take any action to insulate themselves from removal from office. Neither can they act to facilitate control to pass to a friendly party, thereby promoting an inefficient transfer of corporate control. For achieving this, the initiative should be welcomed.

5 SOME PROPOSALS FOR REFORM

While seeking to protect shareholders against fraudulent, coercive or manipulative practices, the law ought to avoid creating barriers to takeover activity unless it can be shown that the benefits of such constraints outweigh the costs.

Through the legislative provisions which prohibit prospective acquirers from concluding hostile takeover transactions as quickly as possible,\textsuperscript{126} current law renders takeovers more risky to mount. It promotes free riding. It gives target firms time and room to manoeuvre and organise resistance. It facilitates competing bids, thus raising the cost of takeovers. It raises the chances of premature leakage of sensitive commercial information, attenuating, in the process, the property rights of searchers. These factors are likely to reduce the incentive to engage in search for takeover targets and be the first bidder.\textsuperscript{127} This is bound to weaken the disciplinary, allocative and wealth creating roles of the hostile takeover process. To assist shareholders and society generally to reap the significant benefits of hostile takeover activity, it is imperative to reform the law. This reform should have as its objective to encourage

\textsuperscript{125} American Law Institute, \textit{above}, n 7 at 385; Bainbridge, \textit{above}, n 45 at 272-5; Berglof & Burkart, \textit{above}, n 7 at 195.

\textsuperscript{126} As to these see the discussion in Part 2 above.

\textsuperscript{127} Winsen, \textit{above}, n 7 at 94.
significant amounts of takeover activity. To bring this about, the law needs to promote
greater protection of the property rights of searchers by ensuring that they fully capture the
returns from investing in information. As well, it should endeavour to facilitate the transfer
of corporate control at the lowest possible cost.128

5.1 Free-rider, cost and related problems.

A rule which permits a bidder to purchase a control block from a private party without first
making an offer to all shareholders (the mandatory bid rule) can assist to achieve these
objectives and consequently improve the functioning of the market for corporate control.129
Therefore, the law governing takeover activity in Australia should be reformed to introduce
such a rule, as recommended by CLERP. Evidently, that rule is bound to have implications
with respect to competitive bidding and, ultimately, the level of the takeover premium
payable on a transfer of corporate control. With respect to this, the law should leave it to
shareholders themselves to determine the level of protection they wish.130 Shareholders of a
company are better informed as to their needs in this respect.131 Those who wish high
premiums should be free to include provisions in their constitution to achieve this. A
properly drafted provision in a company’s constitution can give effect to equal treatment, if
desired. A private solution regarding the distribution of the takeover premium is preferable
to a legally mandated one.132 Because of the diversity of firms and investors, there can be no
uniform optimal solution all the time.133 Some shareholders might prefer high premiums. In

128 See also Hertig & McCahery, above, n 108 at 24.
129 For an exposition of some of the advantages of a mandatory bid rule, see the discussion in Part 3 above.
130 The discussion in this section is adapted in part from my earlier article published in this journal on the
equal opportunity principle. See Mayanja, above, n 32 at 16-18.
131 On this see further Mannolini, above, n 3 at 203-10
132 See further L A Bebchuk, ‘Toward Undistorted Choice and Equal Treatment in Corporate Takeovers’
133 On this see generally Easterbrook & Fischel, above, n 119 at 166; Dodd, & Officer, above, n 7 at 31;
Dodd, above, n 7 at 13-14.
other cases, investors might well conclude that the value of their investment will be maximised by a system of lower premiums.

The *Corporations Act* recognises that shareholders are capable of protecting themselves in corporate control transactions. It leaves companies free to include shark-repellent provisions in their regulations, and so protect their shareholders against partial takeover bids.\textsuperscript{134} The same should be the case with respect to the level of premium. Investors who do not want to take the risk of low premia would then be free to buy shares in companies with regulations that require an auction of the company in the event of a takeover.

### 5.2 Other considerations.

The mandatory bid rule as originally proposed is troublesome in some respects. To remind ourselves, under the CLERP proposal, a bidder would be allowed to acquire in excess of 20% the voting shares of a company on condition that the acquirer announced immediately an unconditional cash offer for all the remaining voting shares in the company. These conditions are designed to protect target shareholders. The requirement that the follow on bid be unconditional is calculated to ensure that the bidder cannot insert in the offer self serving conditions which may enable it to get out of a bid.\textsuperscript{135} The obligation to offer cash, or a cash alternative of equivalent value if it is a scrip offer, is intended to enable interested shareholders to exit the company.\textsuperscript{136} However, these are quite onerous conditions, which are likely to reduce the utility of the original mandatory bid rule proposal.\textsuperscript{137} The proposed rule needs therefore to be refined in these respects.

\textsuperscript{134} See *Corporations Act 2000 (Cth)*, s 648D.
\textsuperscript{136} Ibid, at 107; Hertig & McCahery, *above*, n 108 at 27.
\textsuperscript{137} See also Mannolini, *above*, n 3 at 212.
Because cash must always be offered, the rule will be used only if the prospective acquirer can mobilise sufficient funds to purchase all shares that might be tendered. Needless to say, this is bound to inhibit some transactions which might otherwise be beneficial in cases where the prospective acquirer cannot muster the requisite funds readily. If the mandatory bid rule is to have the desired effect of unleashing more takeover activity, it is advisable to remove this requirement from the rule.

Also, it should not be forgotten that some acquisitions are proscribed unless otherwise sanctioned by certain prescribed authorities. For example, the Trade Practices Act 1974 (Cth) prohibits a takeover if it would have the effect, or be likely to have the effect, of substantially lessening competition in a market, unless the authorisation of the Australian Competition and Consumer Commission is first obtained. This measure is designed to prevent concentration in industry and commerce. In addition, several other legal and administrative initiatives have been implemented with a view to preventing the transfer of ownership of resources from Australian hands without the consent of the Commonwealth Treasurer. As well, there are several limitations on the participation of foreign interests in the control of local firms operating in certain sectors of the Australian economy. By requiring that a mandatory follow on bid must be unconditional, the original CLERP proposal renders participation in the takeover process by bidders who may require regulatory approval

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140 Indeed, proposed takeovers have been successfully opposed on competition grounds in several cases. For a digest of these cases see generally R V Miller, Miller’s Annotated Trade Practices Act 1974, 25th ed 2004, Thomson Lawbook Co, Sydney, at 391-2.
142 See for example the Foreign Acquisitions and Takeovers Act 1975 (Cth), s 21A(2) (restrictions on the acquisition of urban land); Broadcasting Act 1942 (Cth), sections 90G & 92D and Broadcasting Services Act 1992 (Cth), s37 (restrictions on newspaper and electronic media ownership); Treasury, Your Investment in Australia - A Guide For Investors, AGPS, Canberra, 1987 (restrictions on mineral extraction). See further Levy, above, n 25 at 66-70.
more difficult. More seriously, it is apt to unnecessarily restrict the participation of foreign interests in takeover activity in Australia. This is so given especially that where a proposed takeover is opposed by some prescribed authority, the timetable for seeking and securing the necessary approval under the applicable law may not necessarily tie in with the time framework mandated by Chapter 6 of the Corporations Act for conducting takeovers.

Further, and quite importantly, it is important to bear in mind that the ‘national interest’ test applicable under the Foreign Acquisitions and Takeovers Act and the others laws which impose limitations on foreign participation in local industry makes it difficult for prospective bidders to predict with certainty whether or not an application for clearance will, if made, be successful. National interest has been applied variously to issues of economic benefit, the avoidance of monopoly and national security. This introduces a high degree of arbitrariness into the control of foreign takeovers.

In discussing the potential effects of CLERP’s recommended rule, the experience of the United Kingdom, which too has a strict form of mandatory bid rule and on which the proposed Australia rule is modelled is quite instructive. There, the applicable rule requires a person who, through share acquisitions, reaches the threshold of 30% or more of the voting rights of a company to make an offer to acquire the remaining shares. The offer must be in cash or be accompanied by a cash alternative, and may not be made at any price lower than that paid in the previous 12 months. Also, the offer must be unconditional.
It has been observed of this rule that one of its practical effects is to discourage a prospective acquirer from making a market purchase if it wants to maintain conditions to its offer, for example in circumstances where the consent or clearance of third parties is required. It has further been asserted that for this reason, rule 9 bids are rare in the UK. This undermines the utility of the U K mandatory bid rule as a means of promoting hostile takeover activity. Thus, in order to promote a more vigorous market for corporate control, it is prudent to rethink the CLERP proposal with regard to the permissibility of conditional bids in circumstances where regulatory approval is required.

6 CONCLUSION

A mandatory bid rule increases certainty of success of hostile takeover attempts. It can also assist to lower the costs of takeover transactions. By doing this, the rule increases the likelihood of takeovers occurring. As such, the rule has the potential to stimulate more hostile takeover activity. The likely benefits from such increased activity - more efficient management, more efficient allocation of resources within industries and increased shareholder wealth - are likely to far outweigh any loss resulting from reduced takeover premia caused by abandoning the present regulatory regime. From a shareholder and social welfare point of view, therefore, it is advisable to introduce such a rule in Australia.

149 The City Code on Takeovers and Mergers, Rule 9.3. See further Weinberg & Blank, above, n 118 at para 3-934-5.

150 See Button & Bolton, above, n 135 at 118.

151 Id.

152 Some drafting refinements may need to be effected to ameliorate the working of the CLERP proposed rule. On this see Greenwood, above, n 76 at 30-39.
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