THE ROLE OF PROFESSIONAL ADVISERS IN TAKEOVER SITUATIONS

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1. Introduction

1.1 On 28 July 1994 the Commission issued a report in respect of an inquiry it had undertaken into certain aspects of the affairs of Regal Salmon Limited ("the RSL report").[1]

1.2 Chapter 21 of the RSL report (which was entitled "The Role of Professional Advisers in Takeover Situations") considered the issues which can arise when a professional adviser in a takeover situation acts for the target company and is also contracted to provide advice to shareholders of the target company. The chapter concluded by indicating that the Commission intended issuing a paper on the independence of professional advisers in takeover situations. In particular, the Commission indicated that it wished to consider whether more specific guidance, and possibly regulation, might be necessary.

1.3 We have been reviewing the matter. In doing so we have had regard to the relevant policies in other jurisdictions. We have also taken into account recent developments in New Zealand, in particular, the introduction by the New Zealand Stock Exchange ("NZSE") of new Listing Rules on 1 September 1994 and the decision by the Government to defer the introduction of a takeovers code (which contained requirements relating to the role of advisers in takeover situations).

1.4 This paper summarises the relevant aspects of the matter.

2. Background

2.1 It was noted in Chapter 21 of the RSL report that the former NZSE Listing Requirements relating to the role of advisers in takeover situations were not entirely clear.

2.2 Listing Requirement 1.1.3, which dealt with appraisal reports and required the independence of the person issuing the report, was seemingly not applicable in takeover situations. However, Listing Requirement 9.5.2, which was applicable in takeover situations and required directors of the offeree to take independent investment advice if they were in any doubt as to the best interests of the security holders, contained no guidance as to when a person would be considered "independent".[2]

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1 Securities Commission, "Report of an Inquiry into Aspects of the Affairs of Regal Salmon Limited Including Trading in its Listed Securities", Wellington, 1994.

2 A copy of NZSE Listing Requirements 1.1.3 and 9.5.2 is attached at Appendix A. Note that the Listing Requirements were superseded by new Listing Rules on 1 September 1994.

2.3 Thus, it was put to the Commission in the course of the RSL inquiry that:

> *The independent investment advice to directors described in clause 9.5.2 of the Requirements is not an "appraisal report". There is no provision concerning independent investment advice which corresponds to clause 1.1.3. There is, for example, no obligation under clause 9.5.2 to submit independent investment advice to the Exchange for approval, before it is released to security holders. An issuer need only advise security holders and the Exchange of the source and substance of the investment advice.*[3]

3. Views Sought

3.1 In the course of the RSL inquiry the Commission sought the views of a number of market participants as to whether it was appropriate that the same adviser might:

(a) advise the directors of the target on the valuation of the target (in circumstances where the directors anticipated the possibility of a takeover); and

(b) if necessary:

(i) assist in negotiating any offer that might be received; and

(ii) provide an independent report to shareholders on any such offer.

3.2 A further issue raised by the facts before the Commission was whether contingency fees were appropriate in all or any of the above situations.

3.3 The Commission also asked respondents to comment on whether they considered it necessary or desirable that the NZSE Listing Requirements be expanded or clarified to give further guidance in this area.[4]

4. Comments Received

4.1 As noted in the RSL report, we received a range of views from respondents. Of the five substantive replies we received, two took the view that where an adviser is involved in the negotiation of a takeover it is not appropriate for that adviser to also provide an independent report to shareholders on the fairness or otherwise of that offer. Three respondents took the other view.

4.2 A majority of the respondents did, however, indicate that further guidance in, and

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3 Page 177 of the RSL report.

4 Page 180 of the RSL report.

clarification of, the (former) NZSE Listing Requirements would be helpful.[5]

5. General Observations

5.1 Inevitably circumstances will vary from case to case. We think this may be an important cause of the divergence of views amongst respondents. Indeed, the nature of the requirement for independence may depend on the particular circumstances of each case.

5.2 We consider that, as a general rule, the adviser should be unreservedly independent. Thus, in most cases, it will be inappropriate for an adviser to shareholders to have any association with, or interest in, any of the relevant parties or the outcome of the takeover proposal. Moreover, we consider that it will be incumbent, both on the adviser and on the target board, to ensure not only that the adviser is independent in this way but also that there is no other factor which could reasonably be expected to derogate from the perception of that independence.

5.3 However, we believe it is necessary to retain some degree of flexibility to avoid anomalies arising in exceptional cases. An adviser who is associated with the parties or the proposal in certain limited ways may, on occasions, be in a position to provide a balanced report which gives the target company's shareholders the necessary information and guidance, subject to full disclosure of the nature of that association.

6. Overseas Requirements

Australia

6.1 In Australia there is no general requirement that an independent report be provided to shareholders of the target company in every takeover situation. The main requirement for an independent report is under section 648 of the Corporations Law 1990 (Australia). Section 648 requires an independent report only where the offeror is associated in certain limited ways with the target company, for example, where:

(a) the offeror holds 30% or more of, or a class of, the voting shares in the target company; or

(b) the offeror is a director of the target; or

(c) the offeror and the target have common directors.

6.2 There are certain other situations loosely related to takeovers where such a report is also required. In brief, these are:

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5 Page 180 of the RSL report.

(a) pursuant to section 703(5) of the Corporations Law where an acquisition of shares is proposed after the offeror has obtained 90% of the voting shares of the target;

(b) pursuant to section 623 of the Corporations Law in the context of a shareholder's meeting to approve an acquisition of shares by allotment or purchase; and

(c) pursuant to Australian Stock Exchange (ASX) Listing Rule 3J(3) where a listed company proposes to purchase or sell assets of a value in excess of 5% of its total issued capital and reserves and the vendor or purchaser is connected with the company in certain defined ways.

6.3 Thus, it is interesting to note that:

(a) there is no requirement for an independent report in every case; and

(b) there is no requirement for the adviser to be approved by an independent authority in every case.

6.4 The Australian Securities Commission (ASC) has also issued several policy statements which are germane to the issue of the independence of advisers in takeover situations. Of particular relevance are practice notes 42 and 43, and policy statements 74 and 75. The relevant portions of these practice notes and policy statements are set out at Appendix B.

6.5 It may be noted that, in general terms, these practice notes and policy statements recognise that independence is largely a question of fact in each case.[6] It would appear that in situations where the law requires the provision of an independent expert's report (such as those situations outlined in paragraphs 6.1 and 6.2 above), the ASC will insist on a very high degree of impartiality and independence.

6.6 However, the practice notes and policy statements also appear to recognise that full independence or neutrality, while desirable in most cases, will not always be essential. Consider, for example, the following extracts:

> *There might be a current or previous business relationship between the expert and the client or another party interested in the proposal. In this case, where the expert is not expressly prohibited by the Law from preparing an expert's report on the proposal, it is his or her responsibility to ensure the report is unbiased. The closer the relationship between the expert and an interested party, the greater the onus on the expert to demonstrate the absence of bias within the intent of the Law.*[7]
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> *The ASC considers that it is highly desirable that all expert or valuation reports*

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6 See, for example, practice note 42 at paragraph 18 and policy statement 75 at paragraph 14 (see Appendix B).

7 Practice note 42 at paragraph 16 (see Appendix B).

involving the exercise of judgement or opinion should be provided by ***independent*** *experts, whether or not the Law specifically requires that independence. Although the ASC considers that independence is desirable, it realises that there will be times, when the Law does not require independence, that experts who are associated with the company or the proposal, and may provide high quality reports which do adequately inform investors.*[8]

6.7 Interestingly, the practice notes and policy statements also make it clear that when there is some association or relationship between the adviser and the target company or other interested party, that fact should be made quite clear in the report. Thus:

(a) "If a business relationship exists or has existed, the expert should clearly set out the nature and details of the relationship in the report";[9] and

(b) "A relatively small note, towards the end of the report, that the expert is not independent and may receive a success fee is well short of the standards the ASC expects of market participants".[10]

6.8 Finally, insofar as enforcement is concerned, it may be noted that the ASC has the power to initiate prosecutions for breaches of the Corporations Law and to institute civil actions if it is in the public interest to do so.[11]

6.9 Thus, we believe that, in the context of the New Zealand market, the Australian approach:

(a) may be thought to be less flexible. It does not allow each case to be treated on its own merits (note, for example, the approach evident in provisions such as section 648 of the Corporations Law);

(b) is not comprehensive. It applies only in limited situations (for example, those set out in section 648 of the Corporations Law (see paragraph 6.1 above)); and

(c) is not immediate in effect. The statutory procedures are designed to ensure that conflicts are addressed by a process of subsequent investigation and penal enforcement rather than by a process of determination <u>before</u> the report is commissioned.

<u>United Kingdom</u>

6.10 Rule 3.1 of the London City Code on Takeovers and Mergers states that "[t]he board of

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8 Practice note 43 at paragraph 10 (see Appendix B).

9 Practice note 42 at paragraph 17 (see Appendix B).

10 Practice note 43 at paragraph 25 (see Appendix B).

11 See practice note 43 at paragraph 75 for an outline of the relevant provisions (see Appendix B).

the offeree company must obtain competent independent advice on any offer and the substance of such advice must be made known to its shareholders".

6.11 In this regard, three observations may be made.

(a) Firstly, the independent advice required by Rule 3.1 is required to be given to the board of the target company rather than to the shareholders per se. The board only has to make the substance of the report known to shareholders. We note that Rule 3.1 is similar to former NZSE Listing Requirement 9.5.2 (see Appendix A).

(b) Secondly, there is no requirement for advisers to be approved in each case. Nevertheless, it may be noted that under the City Code parties are encouraged to consult regularly with the Panel Executive to obtain a view or a ruling where there is any doubt as to their obligations under the City Code. It appears that, in this way, a de facto system of approval of advisers may operate in practice, although this would rely on parties approaching the Panel Executive (as opposed to the broader obligation to obtain approval in each case).

(c) Thirdly, the notes to Rule 3.1 state that:

> *The requirement for competent independent advice is of particular importance in cases where the offer is a management buy-out or similar transaction or is being made by the existing controlling shareholder or group of shareholders. In such cases, it is particularly important that the independence of the adviser is beyond question.*[12]

6.12 Thus, by inference, it would seem that a certain degree of association between the adviser and the target company may be considered acceptable in other cases. It is interesting to note that this approach is similar to Australia (see paragraph 6.1 above). That is, section 648 of the Corporations Law seems to require full independence or neutrality only where the bidder is associated with the target or its board in some material way.[13]

South Africa

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12 Note 1 to Rule 3.1.

13 See also Rule 3.3 of the City Code which states "[t]he Panel will not regard as an appropriate person to give independent advice a person who is in the same group as the financial or other professional advisor (including a stockbroker) to an offeror or who has a significant interest in or financial connection with either an offeror or the offeree company of such a kind as to create a conflict of interest" (emphasis added). Rule 3.3 also refers to Appendix 3 to the Code. Of relevance, for present purposes is the following statement in Appendix 3:

> *A financial adviser may have the opportunity to act for an offeror or the offeree company in circumstances where the adviser is in possession of material confidential information relating to the other party, for example, because it was a previous client or because of involvement in an earlier transaction. In certain circumstances, this may necessitate the financial adviser declining to act, for example, because the information is such that a conflict of interest is likely to arise. Such a conflict may be incapable of resolution simply by isolating information within the relevant organisation or by assigning different personnel to the transaction; however, when a financial adviser has been actively advising a company which becomes an offeree company, it may be acceptable for it to continue to act* (emphasis added).

6.13 For present purposes, the rules applying in South Africa under the Securities Regulation Panel's Code on Takeovers and Mergers appear to be essentially the same as those applying in the United Kingdom under the London City Code.

7. The New NZSE Listing Rules

7.1 Subsequent to the RSL report, the NZSE has introduced new Listing Rules (on 1 September 1994). It would seem that the NZSE may have taken into consideration the matters raised by the Commission in Chapter 21 of the RSL report in formulating its new Listing Rules. In particular:

(a) The previous differences between former Listing Requirements 1.1.3 and 9.5.2 have now been removed. The new Listing Rules provide that an independent report to shareholders in a takeover situation is an "Appraisal Report" and must meet stricter requirements, for example, in respect of independence.

(b) Pursuant to the Listing Rules, an appraisal report can only be provided by "an independent appropriately qualified person previously approved by the Exchange".[14] Thus, the adviser is approved in each instance and independence is considered on a case by case basis.

(c) The notes to Listing Rule 1.2 (which deals with appraisal reports) make it clear that, in deciding whether or not to approve an adviser any given case, the NZSE will have regard to the sorts of issues that were raised by the Commission in Chapter 21 of the RSL report. The following extracts from the notes to Listing Rule 1.2 are of particular relevance:

> 2. *The Exchange approval required of the person proposed as the reporter, or a person on whom the reporter relies, will be on a case by case basis, so that the Exchange can be satisfied as to the "independence" of the person in question in relation to the circumstances of each case.*
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> 3. *As to independence, the Exchange should be advised when approval is being sought, as to whether:*
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> *(i) the person proposed has had or will have any relationship with the parties to the transactions;*
>
> *(ii) any fee or benefit is payable to that person contingent on the success or implementation of the relevant transaction or any transaction complementary to or dependent on it; and*

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[14] Listing Rule 1.2.1. A copy of Listing Rule 1.2 is attached at Appendix C.

(iii) *that person has had any part in the formulation of the proposal or the transaction or any aspect thereof.*

There may be further queries raised by the Exchange in any instance. For example, the Exchange may take the view that a person who has, or has had, a significant advisory or professional relationship with a party to the transactions or who might otherwise be seen as particularly close to the directors or management, may have at least the appearance of being compromised by the relationship and will not be accepted for appointment by the Exchange.

7.2 For present purposes, it may be noted that advisers will be approved on a case by case basis and that, in considering whether to grant approval, the Exchange will expressly take into account:

(a) whether any fee or other benefit payable to the adviser is contingent on the success or implementation of the proposal;

(b) whether the adviser has had or will have any relationship with the parties to the transaction; and

(c) whether the adviser has had any part in the formulation of the proposal.

7.3 The circumstances in which an appraisal report is required under the new Listing Rules (insofar as takeovers are concerned) are set out in Listing Rule 4.5.8. In short, an appraisal report is required whenever "... any Transferee under a Restricted Transfer is an Insider". It may be noted that, in essence, this is similar to the position under section 648 of the Corporations Law (Australia). That is, an independent report is required whenever the offeror is associated with the target in some way.[15]

7.4 Arguably, however, Listing Rule 4.5.8 goes further than section 648 of the Corporations Law (Australia). For example, pursuant to Listing Rule 4.5.8:

(a) the adviser must be approved by an independent authority (the NZSE) in each case. There is no requirement for approval under section 648 of the Corporations Law;

(b) if the report states that the reporter relies on information provided by, or an opinion expressed by, another party (other than the issuer in question or its directors or employees), that other party must also be approved by the NZSE;[16] and

(c) the word "Insider" is defined as (and, therefore, the requirement for an independent adviser arises whenever):

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15 See paragraph 6.1 above

16 Listing Rule 1.2.1 (see Appendix C).

(i) a director of the target or an "Associated Person"[17] of any such director; or

(ii) a person with "Relevant Information"[18] about the target;

is associated with the offeror. This is wider than the circumstances in which section 648 of the Corporations Law applies (see paragraph 6.1 above).

7.5 However, it should be noted that the scope of Listing Rule 4.5.8 is mitigated to some extent by Listing Rule 4.5.9. Listing Rule 4.5.9 allows the target board to dispense with an appraisal report where a majority of disinterested directors certify that the target shareholders are not at an information disadvantage or that an appraisal report would not materially remedy any such information prejudice. The term "disinterested director" means a director who is not involved in the offer either personally or through an "Associated Person". As noted above, the term "Associated Person" is defined widely.[19]

7.6 Of particular note is that the Listing Rules require advisers to be approved by an independent body on a case by case basis. We support this approach. We believe this approach avoids the need for hard and fast rules and allows each situation to be considered on its merits.

7.7 It should be noted, however, that the new Listing Rules are limited in scope. The Listing Rules apply only to listed companies and, in general terms, apply only where there is some association between the offeror and the target company.[20] In addition, there is an exception in Listing Rule 4.59 (see paragraph 7.5 above).

7.8 We think that issues concerning the independence of advisers in takeovers situations need to be more comprehensively addressed.

8. Deferral of the Takeovers Code

8.1 While the Commission was consulting with market participants in May 1994,[21] the official Government policy was that the Government wished to defer any decision relating to a takeovers code until new companies legislation had been given an opportunity to operate in practice. The inference to be drawn was that the Government believed that the new companies legislation might diminish the need for a takeovers code.

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17 The term "Associated Person" is defined widely in Listing Rule 1.3 (see Appendix D).

18 The term "Relevant Information" is defined in Listing Rule 1.1 (see Appendix E). This definition is similar to the definition of "inside information" in section 2 of the Securities Amendment Act 1988.

19 See Listing Rule 1.3 at Appendix D.

20 See paragraph 7.3 above.

21 See sections 3 and 4 above and page 180 of the RSL report.

8.2 Official Government policy has not changed since that time. In August 1995, the Government decided to defer the introduction of the draft takeovers code released by the Takeovers Panel Advisory Committee ("TPAC") until changes to company law and the new takeover provisions in the NZSE Listing Rules could be assessed.

8.3 The draft takeovers code that was issued by the TPAC in December 1993, and endorsed by the TPAC in June 1995, contained requirements as to the information that was to be supplied to target shareholders. In particular, the draft takeovers code required target directors to obtain a report for shareholders from an independent adviser approved by the TPAC.[22] The TPAC was required to approve each adviser on a case by case basis.

8.4 We believe that the approach adopted by the TPAC:

(a) avoids the need for hard and fast rules or detailed guidelines as to when an adviser is, and is not, "independent"; and

(b) allows for flexibility by enabling each case to be approached on its own merits, but under appropriate supervision.

8.5 In our view, procedures in this general form would be beneficial whether or not there is a takeovers code.

9. Licensing of Advisers?

9.1 There is one further matter which requires brief mention in this paper. Two of the respondents to the Commission's original request for comments suggested that a system of licensing or accrediting of advisers should be instituted.[23] Both respondents were of the view that such a system should be administered by the Securities Commission (rather than the NZSE or some other body).

9.2 We query whether such a formal system would produce any significant net benefits for the market. We doubt that the costs involved in imposing a further layer of regulation of this nature would be justified in terms of a corresponding benefit to the investing public. We envisage these costs would include the cost of compliance for those having to bring themselves within and operate under such a system, and the costs of monitoring and enforcement for the relevant regulatory body.

9.3 We also note that, at present, there is not any statutory mechanism or authority for the imposition of such a regime. Thus, a change to the law would be required.

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22 See rule 9 and clause 19 of the Second Schedule to the draft takeovers code (see Appendix F).

23 See section 3 above.

9.4 Finally, in our view, a system of licensing would not necessarily ensure that the adviser is independent. We think that the approach of the NZSE requiring the adviser to be approved in each case is likely to better achieve the goal of reasonable independence.

9.5 In light of these considerations, we do not recommend a system of licensing of advisers at this time.

10. Opinion Shopping

10.1 We note that the practice of opinion shopping also raises concerns about an adviser's judgement and objectivity. However, we have addressed this in a previous report entitled "Report on Enquiry into a Registered Prospectus Issued by Agricola Resources Limited Dated 3 June 1986" and do not intend to cover this matter in the present paper.[24]

11. Summary and Conclusions

11.1 We believe that professional advisers in takeovers situations should be independent and, moreover, be perceived to be independent. However, we do not think it is desirable to formulate hard and fast rules. A system which allows some flexibility would be preferable to avoid anomalies arising in exceptional situations.

11.2 We note that, at the time of the RSL report, the NZSE Listing Requirements were unclear in this regard.

11.3 The NZSE has now introduced new Listing Rules which appear to address the matters raised by the Commission in Chapter 21 of the RSL report. In particular, we note that the Listing Rules:

(a) specify when an independent report is required;

(b) provide for a determination of the independence of an adviser in each case; and

(c) establish a procedure to determine the independence of an adviser.

11.4 The Commission supports this approach.

11.5 We note, however, that the new NZSE Listing Rules are not comprehensive in scope.

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24 Securities Commission, "Report on Enquiry into a Registered Prospectus Issued by Agricola Resources Limited Dated 3 June 1986", Wellington, 1991. In this case, a promoter obtained different valuations of a kiwifruit property for inclusion in a prospectus. The prospectus failed to disclose that different valuations had been obtained and, in particular, failed to disclose the lowest valuation for the property.

We also note that the New Zealand Society of Accountants has expressed concern about the practice of opinion shopping and has recently issued ED/AES-1, "Advisory Engagement Standard No. 1: Second and Other Opinions", which, in general, outlines the procedures that must be followed when parties other than ongoing clients ask for an opinion on accounting and reporting matters.

For example, they apply only where the target company is a listed company. Moreover, in general, they apply only where there is an association between the offeror and the target, that is, where the market perceives a special risk that the transaction may not be at arms length.

11.6 The Commission believes that guidance should be readily available on the independence of professional advisers in takeover situations where the target is a non-listed company. The Commission understands that the takeovers code was expected to address this.

11.7 We are referring are a copy of this paper to the various industry organisations which are involved in the business of offering valuation and associated advisory services. A list of names is included at Appendix G. The Commission invites these bodies to review their rules and consider whether it is desirable to offer better guidance to their members on questions relating to the independence of advisers in takeover situations, along the lines of the principles set out in this paper, in the interests of the advisory industry and the securities market in general.

6 November 1995

1.1.3 Appraisal Report

An Appraisal Report for the purposes of these Requirements shall:

(Amended: 1.2.91)

(a) be made by an independent appropriately qualified firm, or person previously approved by the Exchange[1];

(Amended: 1.2.91)

(b) be addressed to the Directors of the Issuer not associated with any relevant Associated Persons, or, if there are no such Directors, to the Exchange which at the expense of the Issuer, will oversee the distribution of the report to the shareholders in general;

(c) be for the benefit of the Equity Security Holders of the Issuer not associated with any relevant Associated Persons;

(d) state whether or not in the opinion of the reporter the consideration and the terms and conditions of any proposed Issue or transaction with any relevant Associated Persons are fair to the Equity Security Holders other than those associated with the relevant Associated Persons;

(e) state whether the reporter has obtained all the information it believes desirable for the purposes of preparing the report including all relevant information which is or should have been known to any Director of the Issuer and made available to the Directors;

(f) state any material assumptions on which the reporter's opinion is based;

(g) state any term of reference which may have materially restricted the scope of the report; and

(Amended: 1.2.91)

(h) be accompanied, if a summary only of the report is to be provided to the beneficiaries of the report, by a certificate of the reporter that the summary is accurate and not misleading to the beneficiaries of the report in all the circumstances likely to be generally known by the beneficiaries; and

(Amended: 1.2.91)

(i) shall not contain a general disclaimer purporting to absolve the reporter from liability for the opinion expressed in the report, although a reporter may disclaim liability to the extent to which reasonable reliance on information provided by others or on assumptions disclosed in the report or reasonably taken as implicit, proves to be misplaced.

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(1) 1. The Exchange approval required of the "independent appropriately qualified firm or person" proposed as the reporter will be on a case by case basis, so that the Exchange can be satisfied as to the "independence" of the reporter in relation to the circumstances of each case. However, the Exchange will not approve any person who is or has been in an audit relationship with any party to the transaction.

(Amended: 1.2.91 and 30.3.92)

2. The attention of all prospective reporters is drawn to any guidelines which the Exchange might put in place or might be published by other professional bodies.

3. As to independence, the Exchange should be advised when approval is being sought, as to whether:

(i) the reporter has had or will have any relationship with the parties to the transaction;

(ii) any fee or benefit is payable to the reporter contingent on the success or implementation of the relevant transaction or any transaction complementary to or dependent on it;

(iii) the reporter has had any part in the formulation of the proposal of the transaction or any aspect thereof.

There may be further queries raised by the Exchange in any instance. For example, the Exchange may take the view that any reporter whose relationship with any party to the transaction has involved or may involve in the future a significant advisory role or who might otherwise be seen as particularly close to the directors or management may have at least the appearance of being compromised by the relationship and will not be accepted for appointment by the Exchange.

For the purposes of the foregoing:

(Amended: 1.2.91)

(j) "relevant Associated Persons" means the Associated Persons whose association or connection with the Issuer, or the Directors of the Issuer, or with the parties to a transaction or the anticipated acquirors of the Securities of an Issue would result in a requirement that an appraisal report be obtained under these Requirements;

(Amended: 1.2.91)

(k) in forming and expressing an opinion as to the fairness of a proposal for the purpose of clause 1.1.3(d) the reporter shall have regard to and mention any alternative means or avenues for acquisition or disposition of assets or services or subscription for an Issue the subject of the report, as the case may be, which seem to the reporter to be reasonably available to the Issuer. The reporter shall disregard any constraints arising from indications by the Directors that such alternative courses are not acceptable, or that they would not propose to pursue them, if any such reasons may be wholly or partly attributable to concerns about the interests of the relevant Associated Persons in distinction to the interests of the other Equity Security Holders.

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9.5 OBLIGATIONS OF OFFEREES IN TAKEOVERS(1)

9.5.1 Information to Security Holders

Every Offeree shall give to all of its Directors and Equity Security Holders sufficient information to enable them to make an informed investment judgement and shall state the source of the information.

9.5.2 Independent Investment Advice

If the Directors of an Offeree, having considered all relevant effects including the present price of the Issuer's Securities on the market, its past record and its immediate prospects, are in any doubt as to the best interests of the Security Holders, they should take independent investment advice. If outside advice is taken, Security Holders and the Exchange should be advised of its source and substance.

9.5.3 Directors Not to Thwart Offer

The Directors of an Offeree are not to take action to thwart an offer unless they honestly believe that acceptance is not in the best interests of Security Holders. If the Directors consider the offer is too low, or believes on reasonable grounds that a higher offer is in prospect, they should so advise Security Holders. The seeking of a higher offer is to be confined to one reasonably in prospect and is not to be unduly prolonged or used purely as a device to thwart or delay an unwelcome bid.

9.5.4 Restriction on Issue of Voting Securities

Except in the case of a decision made prior to and not in contemplation of an offer, unallotted Voting Securities shall not be issued, following knowledge of an offer, without the sanction of a general meeting of Security Holders, which shall be held as soon as practicable.

(1) *The Directors of the Offeror and the Offeree (and their advisers) have a primary duty to act in the best interest of their respective companies' Security Holders. They must not allow themselves to be influenced by considerations of personal or family shareholdings, or their position or personal relationship with the Companies or individuals concerned.*

Appendix B

PRACTICE NOTES AND POLICY STATEMENTS OF THE AUSTRALIAN SECURITIES COMMISSION

In the RSL report, we reviewed the practice notes and policy statements of the Australian Securities Commission to see how that Commission had dealt with the issue of adviser independence.

Practice Note 42 - "Independence of Experts' Reports"

Practice Note 42, "Independence of Experts' Reports", issued on 8 December 1993, includes:

> RELATIONSHIP BETWEEN EXPERT AND INTERESTED PARTIES
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> 16. There might be a current or previous business relationship between the expert and the client or another party interested in the proposal. In this case, where the expert is not expressly prohibited by the Law from preparing an expert's report on the proposal, it is his or her responsibility to ensure the report is unbiased. The closer the relationship between the expert and an interested party, the greater the onus on the expert to demonstrate the absence of bias within the intent of the Law.
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> 17. If a business relationship exists or has existed, the expert should clearly set out the nature and details of the relationship in the report.
>
> 18. The ASC may enquire into any case where an expert's past or present business relationship with an interested party creates the perception that the expert is not disinterested, thereby undermining the report's credibility. The expert's independence can only be determined in relation to a particular case. However, he or she should seriously consider declining to accept an engagement as an expert on a proposal if he or she, or a related person:
>
> (a) is a substantial creditor of an interested party or has any other financial interest in the outcome of the proposal;
>
> (b) has participated in strategic planning work for the client or any other interested party (for example, by advising on possible acquisitions by takeover); or
>
> (c) acts as lawyer, banker, financial consultant, tax adviser or accountant etc to the client or any other interested party (other than providing professional services strictly for compliance purposes rather than strategic or operational decisions or planning).
>
> 19. An expert is not precluded from providing a report merely because, during the preceding two years, he or she:
>
> (a) acted as auditor of the target corporation, the client or any other interested party;

(b) worked for a corporation which deals in the money market as part of its ordinary business and may hold bills of exchange or promissory notes the client or other interested party may be liable for; or

(c) worked for a corporation that manages an investment portfolio that includes shares in the client or any other interested party.

These criteria do not necessarily denote or imply independence. The expert may need to demonstrate his or her independence in any particular case.

Practice Note 43 - "Valuation Reports and Profit Forecasts

Practice Note 43, "Valuation Reports and Profit Forecasts", issued on 8 December 1993, includes:

Independence

10. The ASC considers that it is highly desirable that all expert or valuation reports involving the exercise of judgement or opinion should be provided by **independent** expert, whether or not the Law specifically requires that independence. Although the ASC considers that independence is desirable, it realises that there will be times, when the Law does not require independence, that experts who are associated with the company or the proposal, and may provide high quality reports which do adequately inform investors.

11. Independent experts will provide security holders and investors with an objective and unbiased assessment, independent of any interested party (including any associate or an interested party) and sufficient information to make an effective, informed decision. Where an expert is not independent, the readers of the report have reason to expect the expert to disclose his or her lack of independence. As readers do have such reasonable expectations the expert is under a duty to disclose any interests. Failure to do so may constitute misleading or deceptive conduct under s995 of the Law.

12. For any report to be described as independent the expert must be independent of the company which is subject of the report. In a takeover, he or she must be independent of the offeror and the board of the target company. In an offer of securities, he or she must be independent of the promoter or the vendor.

25. A relatively small note, towards the end of the report, that the expert is not independent and may receive a success fee is well short of the standards the ASC expects of market participants. Neither the expert nor the commissioning party should condone such lip service to disclosure.

75. The ASC has the power to initiate prosecutions for breaches of the Law and has the power under s50 of the ASC Law to institute civil actions if it is in the public interest to do so.

Policy Statement 75 "Independent Expert Reports to Shareholders"

Policy Statement 75, "Independent Expert Reports to Shareholders", also issued on 8 December 1993, includes:

> INDEPENDENCE
>
> 14. The expert may not be associated with the offeror or the target company. Whether a person is associated with the offeror or the target company, and is therefore precluded from acting as an expert under s648(1), is a question of fact ...
>
> 15. Under s648(2), the expert must disclose the existence of any other business relationship with the offeror or the target company or any of their associates which, while not precluding him or her from acting as an expert under s648(1), would be material to assessing the expert's impartiality. The expert should also disclose any intention to establish future business relationships with the offeror or target.
>
> 16. Prior to commencing work, the expert should obtain written instructions which set out the proposal to be assessed, respect his or her independence, recognise his or her right to refuse to provide an opinion or report at all, if not provided with the information and explanations he or she requires to prepare the report, grant him or her the same access to the company's records as its auditor would have and provide for a fee which is in no way contingent upon the success or failure of the takeover.
>
> 17. If the expert is not provided with the access to the company's records, to the extent mentioned earlier, or is given unduly short time relative to the statutory time constraints, he or she should consider refusing to provide a report at all, rather than providing an unsatisfactory report and attempting to deal with its deficiencies by disclaiming responsibility for them.

1.2 APPRAISAL REPORTS

1.2.1 Approval by Exchange: An Appraisal Report for the purposes of the Rules shall be made by an independent appropriately qualified person previously approved by the Exchange. If the report states that the reporter relies on information provided, or an opinion expressed, by another party (other than the Issuer in question or its Directors or employees) that other party shall also be approved by the Exchange.

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1. **Appraisal Reports are required by Rules 4.5.8, 6.2.2 and 9.2.5.**

2. **The Exchange approval required of the person proposed as the reporter, or a person on whom the reporter relies, will be on a case by case basis, so that the Exchange can be satisfied as to the "independence" of the person in question in relation to the circumstances of each case.**

3. **As to independence, the Exchange should be advised when approval is being sought, as to whether:**

   (i) the person proposed has had or will have any relationship with the parties to the transaction;

   (ii) any fee or benefit is payable to that person contingent on the success or implementation of the relevant transaction or any transaction complementary to or dependent on it;

   (iii) that person has had any part in the formulation of the proposal of the transaction or any aspect thereof.

   There may be further queries raised by the Exchange in any instance. For example, the Exchange may take the view that a person who has, or has had, a significant advisory or professional relationship with a party to the transaction or who might otherwise be seen as particularly close to the directors or management, may have at least the appearance of being compromised by the relationship and will not be accepted for appointment by the Exchange.

1.2.2 Contents of Report: An Appraisal Report shall:

(a) be addressed to the Directors of the Issuer not associated with any relevant Associated Persons, or, if there are no such Directors, to the Exchange, which at the expense of the Issuer will oversee the distribution of the report to holders of Securities of the Issuer. For this purpose "relevant Associated Persons" means the Associated Persons whose association or connection with the Issuer, or the Directors of the Issuer, or with the parties to a transaction or the anticipated acquirers of the Securities of an issue, results in a requirement that an Appraisal Report be obtained under the Rules;

(b) be expressed to be for the benefit of the holders of Equity Securities of the Issuer not associated with any relevant Associated Persons (as defined in (a));

(c) state whether or not in the opinion of the reporter the consideration and the terms and conditions of the relevant proposed issue or other transaction are fair to the holders of Equity Securities other than those associated with the relevant Associated Persons (as defined in (a));

(d) state whether or not in the opinion of the reporter the information to be provided by the Issuer to holders of its Securities is sufficient to enable holders to understand all relevant factors, and make an informed decision, in respect of the question referred to in (c);

(e) state whether the reporter has obtained all information which the reporter believes desirable for the purposes of preparing the report, including all relevant information which is or should have been known to any Director of the Issuer and made available to the Directors;

(f) state any material assumptions on which the reporter's opinion is based;

(g) state any term of reference which may have materially restricted the scope of the report; and

(h) if it contains a disclaimer of liability, not purport to absolve the reporter from liability for an opinion expressed recklessly or in bad faith.

If the reporter forms the opinion that the relevant issue or other transaction has been structured wholly or partly with a view to conferring a benefit on the relevant Associated Persons (as defined in (a)), the reporter may have regard to, and mention, any alternative courses for acquisition or disposition of assets or services, or subscription for an issue, as the case may be, which seem to the reporter to be reasonably available to the Issuer. The reporter shall disregard any constraints arising from indications by the Directors that such alternative courses are not acceptable, or that they would not propose to pursue them, if any such reasons may be wholly or partly attributable to concerns about the interests of the relevant Associated Persons in distinction to the interests of the other holders of Equity Securities.

1.2.3 **Summary of Report:** An Issuer may, if it so elects, circulate to holders of its Securities a summary of an Appraisal Report, rather than the report in full. If the Issuer elects to circulate a summary then that summary shall be accompanied by a certificate from the reporter that the summary is accurate and not misleading to the beneficiaries of the report in all the circumstances likely to be generally known by the beneficiaries.

1.3 ASSOCIATED PERSONS

1.3.1 **Associated Persons:** In the Rules, a person is an Associated Person of another person if the first person is associated with the other person in terms of Rules 1.3.2 to 1.3.6.

1.3.2 **Association:** A person (the "**first person**") is associated with another person (the "**second person**") if, in making a decision or exercising a power affecting an Issuer, the first person could be influenced as a consequence of an Arrangement or relationship existing between, or involving, the first person and the second person.

1.3.3 **Deeming Provisions:** Without limiting Rule 1.3.2, the first person is associated with the second person if:

(a) the first person is a company, and the second person is:

(i) a Director of that company; or

(ii) a Related Company of that company; or

(iii) a Director of a Related Company of that company; or

(b) the first person is a spouse, domestic companion, child or parent of the second person, or a nominee or trustee for any of them or for the second person; or

(c) the first person is a Director of a company, or holds a relevant interest (as defined in sections 5 and 6 of the Securities Amendment Act 1988) in Securities carrying more than 10% of the votes of a company and the first person and the second person are parties to an Arrangement relating to the control of, or the control or ownership of securities in, that company, which Arrangement affects Securities of that company carrying more than 30% of the total votes attaching to Securities of that company; or

(d) the first person and the second person are acting jointly or in concert; or

(e) the first person and/or the second person propose to do, or are likely to do, anything which will cause them to become associated in terms of (a) to (d) or Rule 1.3.2.

1.3.4 **Exclusions:** The first person is not associated with the second person solely because:

(a) the first person acts as a professional or business adviser to the second person, without a personal financial interest in the outcome of that advice; or

(b) the first person is a Broker or other person whose ordinary business includes dealing in Securities on behalf of others, and the first person acts in accordance with the specific instructions of the second person to deal in Securities; or

(c) the first person acts as a proxy or representative of the second person for the purposes of a meeting of holders of Securities of a company or other entity.

1.3.5 **Reverse Application:** If the first person is associated with the second person in terms of Rules 1.3.2 to 1.3.4, then the second person shall be deemed to be associated with the first person.

1.3.6 **Ruling:** Notwithstanding anything in this Rule 1.3, persons shall not be associated if the Exchange rules that they are not associated.

1.3.7 **Definition:** For the purposes of this Rule 1.3, "**Arrangement**" means an agreement, arrangement, or understanding, whether express or implied, and whether or not legally enforceable.

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1. **The definition of "Associated Person" is broad. If there is any doubt as to whether any two or more persons are Associated Persons, Issuers should seek a ruling from the Exchange in terms of Rule 1.3.6.**

2. **If a connection between two persons of the nature referred to in Rule 1.3.3(c) or (d) is not related to the matter in respect of which the question of whether those persons are Associated Persons is required to be determined, the Exchange will readily grant a ruling that those persons are not Associated Persons.**

"**Relevant Information**" means at any time information received or generated and held by an Issuer about its undertaking, activities, business environment, prospects, financial position, or financial performance which is not reasonably available to an informed investor in the market in a form substantially as useable as the form in which it is available to the Issuer, and which upon disclosure to the market would, or would be likely to, affect materially the market price of any of the Issuer's Quoted Securities.

Appendix 4

DRAFT TAKEOVERS CODE

RULE 9

9. Independent advice on the merits of an offer

The directors of a target company shall obtain a report from an independent adviser approved by the Panel on the merits of an offer.

CLAUSE 19 OF THE SECOND SCHEDULE

19. Independent advice on the merits of an offer

The identity of the independent adviser who has provided a report under Rule 9 of the Code and a copy of the adviser's report or a summary of the report prepared by the adviser and a statement that the full report is available for inspection at a stipulated address and that a copy of the report will be sent to any offeree upon request and payment of a stipulated fee which shall not exceed the cost of copying and posting the report.

The report and summary report shall include a statement of the qualifications and expertise of the adviser and particulars of any interests of the adviser that could affect the adviser's ability to provide an unbiased report.

Appendix G

We have referred a copy of this paper to the following industry organisations which are involved in the business of offering valuation and associated advisory services:

Arbitrators Institute of New Zealand Inc;
International Association of Financial Planners;
Major investment banks/investment advisers;
Major law firms;
New Zealand Institute of Surveyors;
New Zealand Institute of Quantity Surveyors
New Zealand Society of Accountants;
New Zealand Institute of Architects;
New Zealand Law Society;
New Zealand Engineers Federation;
New Zealand Institute of Valuers; and
New Zealand Stock Exchange.