M&A Meltdowns: Unravelling the lessons from failed M&A deals

MinterEllison.

Contents

Introduction

The overwhelming majority of take-private deals that are publicly announced and recommended by the boards of ASX listed targets successfully close. Control usually passes over the ensuing months either to the acquirer who 'bounced the ball' with the first recommended offer or to another party who makes a subsequent, unmatched superior offer.[i]

Despite this track record of success, the Australian corporate landscape has become littered over time with failed take-private deals – ones that that were publicly announced with a unanimous recommendation from the target's board, endorsed by an independent expert but ultimately failed to complete.

In the wake of these failed 'friendly' deals, the prospective acquirer and/or the target board (let alone its shareholders) are often left dismayed by a public process that was initially announced with ebullience and promise, unfolded over months but then suffered an imploding event.

The Australian market has recently seen a proliferation of failed 'friendly' take-private deals. The most recent high profile example is **EIG / Brookfield's failed attempt to acquire Origin Energy** – a deal that was voted down by influential shareholder AustralianSuper along with a handful of other key shareholders. This was despite multiple prior price increases, a unanimous recommendation from the Origin Board and even a final offer price that was above the top end of the independent expert's valuation range.

In the aftermath of any failed public deal, one or more of the parties are often left licking their wounds with substantial sunk costs in terms of advisory fees and lost management time, other foregone alternative opportunities, as well as reputational impacts. Plenty of sobering lessons have been served up in failed Australian take-private deals over the past 15 years – sometimes these lessons have not been heeded, with a recurrence of the same or similar mistakes.

What then are the lessons that can be drawn from these failed 'friendly' deals? What can prospective acquirers, target boards and their key shareholders learn from them? We unpack the lessons for all three stakeholder groups, drawing not only from recent failed take-private deals but also ones whose ashes still smoulder after more than a decade and that live long in the corporate memory. We also draw on lessons from take-private deals that were on the cusp of failure but got over the line due to a proactive and effective response to the potentially terminal challenges they were facing.

The unifying theme of these lessons is that public market deals are imbued with execution risks, meaning that each stakeholder group needs to be flexible and pragmatic in anticipating and responding to those risks, noting that although the risks are different for each group they overlap in several respects.

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Snapshot of failed 'friendly' deals announced between 2007 – 2023 (non exhaustive)

Year[ii]	Target	Prospective acquirer	Transaction structure	Cause of failure
2023	Origin Energy	EIG / Brookfield	Scheme	Institutional shareholder activism from AustralianSuper (blocking stake acquired and voted against the scheme)
2023	Liontown Resources	Albemarle	Scheme (but non-binding indicative proposal only)	Industry competitor activism from interests associated with Gina Rinehart (blocking stake acquired, Albemarle withdrew its proposal citing "growing complexities associated with executing the transaction")
2023	Essential Metals	IGO and Tianqi Lithium	Scheme	Industry competitor activism from Mineral Resources (blocking stake acquired and voted against the scheme)
2022	Alliance Aviation Services	Qantas	Scheme	Regulatory approval (ACCC) not obtained
2022	Nitro Software	Alludo	Dual track scheme and takeover	Scheme vote failed due to 19.9% stake held by competing bidder (Potentia) who voted against the scheme Takeover failed because Alludo made an unqualified 'best and final price' statement – the next day, the competing bidder - Potentia - made an offer marginally above Alludo's 'best and final' price
2021	Link Group	Dye & Durham	Scheme	Regulatory approval (UK FCA) not obtained.[iii]
2021	AGL	N/A (this was a demerger)	Scheme	Environmental shareholder activism from Mike Cannon-Brookes
2020	CML Group (now Earlypay Ltd)	Scottish Pacific	Scheme	Mutually terminated after a dispute with bidder regarding alleged material adverse change

Snapshot of failed 'friendly' deals announced between 2007 – 2023 (non exhaustive)

Year[ii]	Target	Prospective acquirer	Transaction structure	Cause of failure
2019	Pioneer Credit	Carlyle Group	Scheme	Terminated by target after dispute with bidder regarding alleged material adverse change
2018	APA	CK Group	Scheme	Regulatory approval (FIRB) not obtained
2014	Horizon Oil	Roc Oil	Scheme	Acquirer was able to withdraw (without penalty) because it received a superior offer only days before Roc Oil scheme meeting – leaving Horizon Oil 'high and dry' with a failed deal, significant sunk costs and zero compensation from its suitor.
2011	Redflex	Macquarie and Carlyle Group	Scheme	Shareholder activism from former Chairman Chris Cooper who held a material pre-existing key stake and voted against the scheme
2011	Flinders Mines	Magnitogorsk Iron and Steel Works OJSC (MMK), a Russian company	Scheme	Failure of the following condition before sunset date: *No temporary restraining order, preliminary or permanent injunction or other order issued by any court of competent jurisdiction or other legal restraint or prohibition being in effect at 8.00 am on the Second Court Date which prevents the consummation of any aspect of the Scheme* Ms Elena Nikolayevna Egorova, a shareholder in MMK, brought an action in the Chelyabinsk court challenging the legitimacy of the MMK board's resolutions relating to MMK's proposed acquisition of Flinders. On 30 March 2012, the Chelyabinsk court issued an injunction restraining MMK from proceeding with its proposed acquisition of Flinders. The injunction was appealed by MMK and Flinders but the appeals failed (i.e. the injunction was upheld). The sunset date passed and was not extended. MMK walked away from the deal without penalty. Flinders was left with substantial sunk costs
2009	Indophil Resources	Zijin Mining	Takeover	Terminated by mutual agreement in response to persistent delays (more than seven months) in obtaining required Chinese regulatory approvals
2007	Symbion	Healthscope	Scheme	Industry competitor activism from Primary Healthcare (blocking stake acquired and voted against the scheme).[iv]

Lessons for prospective acquirers

Prospective acquirers need to navigate three key stakeholders to achieve deal success – the target board, the target shareholders and regulatory authorities. Potential pitfalls across each of these gatekeepers await at every turn.

Lesson 1: Select your target carefully and construct your offer appropriately

Target selection has a crucial bearing on deal success. For example, if the target's board and/or its share register has a strong representation from founders and/or management shareholders, then lobbing an all-cash offer – even one at a significant premium to the prevailing market price –may not be sufficiently compelling for these key shareholders, as they typically view the offer through a longer term value lens.

The prospective acquirer needs to be open to offering founder/management shareholders rollover equity, so they can continue to hold and grow their investment – and potentially extending that same opportunity to all other shareholders (safe in the knowledge that it is rarely attractive for institutional and retail shareholders to roll over their investment into an unlisted vehicle).

Similarly, if the target has one or more long-term key institutional shareholders, engaging with them and securing their support before going public goes a long way to assuring deal success. This applies equally to the target board before they throw their public support behind a deal. See further Lesson 2 below for target boards.

Apart from analysing the composition of the target's share register, a prospective acquirer should have a compelling strategic proposition to 'sell' to the target board. For example, identifying a target company that is in a growth phase, has already tapped equity and debt capital markets to fund its growth, but requires further funding. A prospective acquirer that can fund and accelerate the target's growth plans away from the ASX, rather than dramatically change those plans, is likely to be attractive to a target's board to de-risk its growth strategy.

Example

Healthia had an aggressive roll-up strategy, buying up optometry, podiatry, physiotherapy and hand therapy clinics with 340 businesses across Australia and New Zealand. But Healthia was in a challenging position as an ASX listed company; there were only so many rights issues that shareholders could absorb and so much debt it could borrow to continue its growth trajectory as a publicly listed company. Identifying Healthia's growth aspirations, private equity firm Pacific Equity Partners (PEP) presented the Board with a take-private offer that would allow Healthia to fund the company's growth plans away from the ASX. PEP offered roll-over equity to the founders, management and all other existing shareholders. PEP ended up with a 75% stake, effectively providing a private capital solution for management, who together with other shareholders retained the other 25%. That structure mirrors previous PEP deals at Patties Foods (2016) and IT services company Citadel Group (2020).

A prospective acquirer would also do well to **seek out target companies with a strong track record of defensive earnings** – InvoCare, Estia, Healthia and Costa, for example. It is easier to arrange debt funding, and have a higher degree of certainty that you can meet internal rate of return metrics for the prospective acquirer's board, investment committee and underlying investors. Of course, if the target is attractive to one prospective acquirer, it is likely to be attractive to many others, so the following lessons are also apt.

Lesson 2: Be prepared to increase your price after going public - in response to material changes in financial performance (either the target's or yours!)

Public market deals typically take several months to consummate after they are first publicly announced – especially if complex regulatory approvals are needed. In the months after public announcement, the target's financial performance can improve dramatically, with the potential to materially disrupt the prospective acquirer's initial pricing (and associated funding arrangements).

That improvement will become public as part of the target's regular reporting and disclosure obligations. Material improvement in the target's financial performance between initial announcement and scheduled implementation may cause its board, key shareholders and/or the independent expert to reconsider their initial support for the proposed deal.

Example 1

In late 2021, Western Areas entered into an implementation agreement with IGO under which IGO agreed to acquire all of the shares in Western Areas by way of a scheme of arrangement for $3.36 cash per Western Areas share. KPMG, the independent expert appointed by Western Areas to opine on whether the scheme was in the best interests of Western Areas' shareholders, initially proposed to conclude that the transaction was fair and reasonable. However, following a significant increase in the then current and projected medium to long-term nickel prices (partly attributable to the impact of the Russia/Ukraine conflict on the supply of nickel), KPMG proposed to conclude that the transaction was NOT fair and reasonable. In response, the target board withdrew its public recommendation of the scheme and engaged with IGO with a view to securing a revised offer that adequately reflected the improved outlook for nickel prices. Following this engagement, IGO agreed to increase the scheme consideration to $3.87 cash per share - a 15.2% premium to the initial scheme consideration - which was sufficient to get the target board and shareholders across the line. However, since implementation of the transaction in 2022 the nickel price (upon which the enhanced scheme consideration was founded) has deteriorated significantly which appears to have contributed to IGO recently announcing an estimated write down of up to $190 million of the assets acquired under the Western Areas scheme. Accordingly, while this example provides a clear illustration that prospective acquirers may need to increase their offer to be successful in the face of improved financial performance or prospects of a target - equally, it should serve as a cautionary tale against doing so lightly without adequate consideration of the potential downside risks, particularly where the value of the target is tied to volatile commodity prices determined by external macroeconomic forces.

Example 2

On 27 March 2023, Origin Energy entered into an implementation agreement with a consortium comprising Brookfield and EIG under which the consortium agreed to acquire all of the shares in Origin by way of a scheme of arrangement for $8.912 cash per share, consisting of Australian dollar and US dollar components. This fell within the valuation range of $8.45 to $9.48 subsequently assessed by the independent expert, Grant Samuel. In the latter half of 2023, Origin released a series of ASX announcements detailing improved financial performance and favourable projections for FY24. At around this time, Origin's largest shareholder AustralianSuper made a public statement to the effect that the consortium's offer undervalued Origin's shares and that it intended to vote its holding against the scheme at the scheme meeting. In light of the improved financial outlook for Origin and seemingly with a view to secure the affirmative vote of AustralianSuper, the consortium increased the scheme consideration to $9.53 per Origin share which it declared was its 'best and final' price, subject to no superior proposal emerging. Despite this exceeding the independent expert's valuation range for Origin shares, AustralianSuper swiftly announced that the consortium's improved offer remained 'substantially below' its estimate of Origin's 'long-term value' and used its more than 17% shareholding to vote down the scheme at the scheme meeting (see Lessons 4 and 6 for a further discussion of the Origin transaction in the context of shareholder activism and the implications of 'best and final' statements).

Lesson 2 (continued): Be prepared to increase your price after going public - in response to material changes in financial performance (either the target's or yours!)

If the acquirer is itself listed and is offering its own scrip to target shareholders as consideration, any material and sustained deterioration in the acquirer's share price after the deal is initially announced will mean target shareholders will be receiving less implied value than what was originally presented to them at the time of initial announcement. This may cause the target board, its key shareholders and or the independent expert to reassess whether the scrip consideration needs to be increased to retain the equivalent implied value that was offered at the time of initial announcement.

Example 1

In 2018, Tokyo listed LIFFUL acquired ASX listed Mitula under a scheme where Mitula shareholders would receive default consideration comprising a combination of cash and LIFFUL listed scrip or, if they made an all-scrip election, all LIFFUL shares. There was a mechanism to protect Mitula shareholders from a decrease of up to 10.78% in the LIFFUL share price. This mechanism involved a corresponding increase in the agreed share exchange ratio, so as to maintain the implied value of the scrip consideration as at the date of initial announcement to compensate for any downward movement of up to 10.78% in the LIFFUL share price. When the scheme was first announced on 9 May 2018, the implied value of the scrip consideration was A$0.85 per Mitula share. In the week before the scheme booklet was issued on 23 October 2018, the implied value of the scrip consideration had fallen significantly to A$0.605 per Mitula share, due to volatility in the AUD/JPY exchange rate and a decline in the LIFFUL share price. This was well beyond the price protection mechanism referred to above. In response to negative feedback received from Mitula shareholders ahead of the scheme meeting and pressure from the Mitula Board, LIFULL provided a cash top up amount to respond to the falling value of LIFULL scrip.

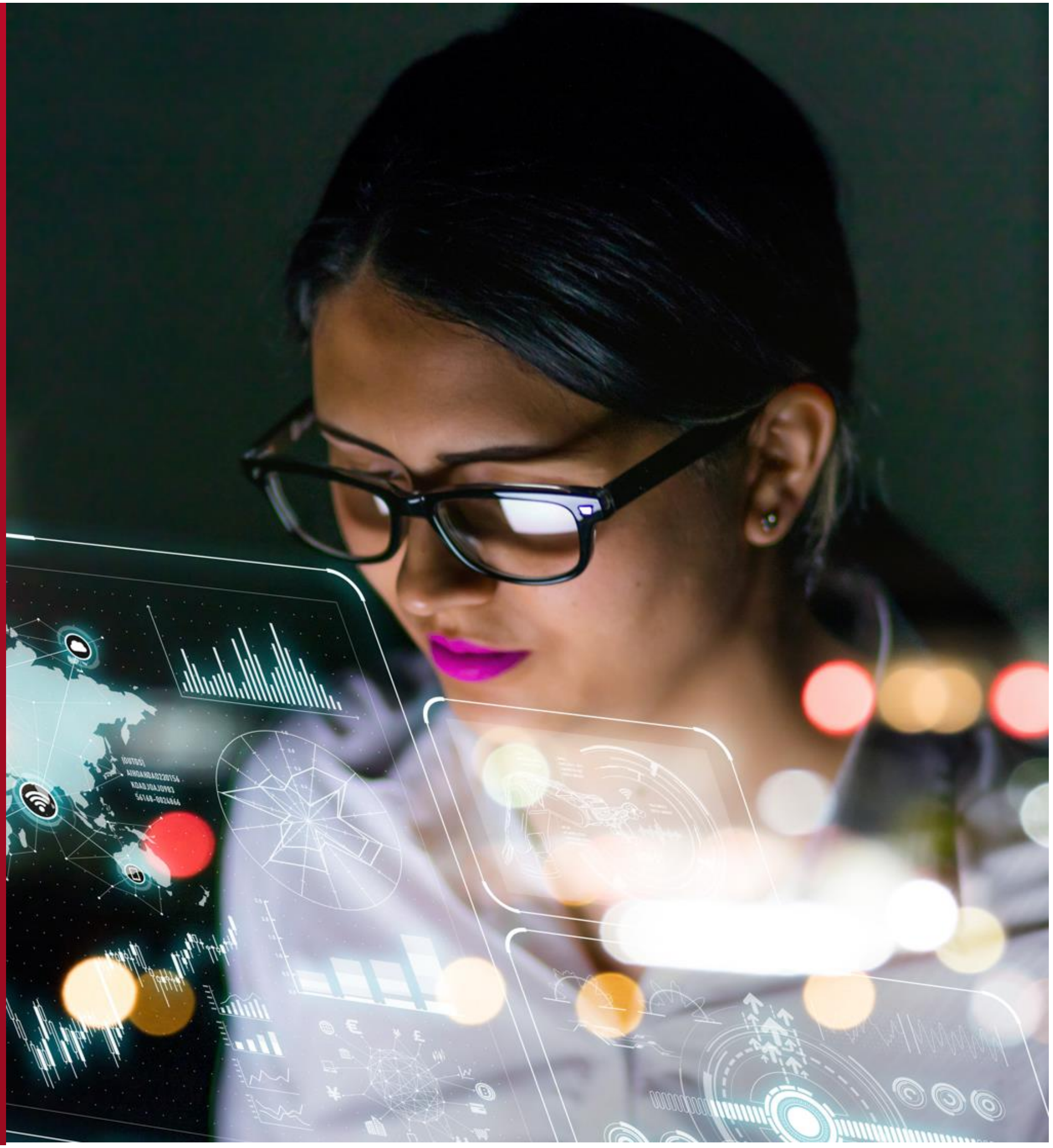
Example 2

Also in 2018, Paris listed Unibail-Rodamco acquired ASX listed Westfield under a scheme where Westfield securityholders would receive a combination of cash and stapled securities in Unibail-Rodamco. When the scheme was first announced on 12 December 2017, the implied value of the scheme consideration was A$10.01 per Westfield security. In the days just before the scheme booklet was issued on 12 April 2018, the implied value of the scheme consideration had fallen to A$8.99, due to volatility in the exchange rate and decline in the Unibail-Rodamco share price. Indeed, the implied value continued to deteriorate in the lead up to the scheme meeting on 24 May 2018, resulting in public pressure being applied to Unibail-Rodamco to increase the scheme consideration – which it did not do. Westfield securityholders ultimately approved the merger.

Lesson 3: Be prepared to increase your price after going public, in response to a host of other developments

A prospective acquirer also needs to stand ready to consider increasing its price after public announcement in response to a host of potential developments including:

- the emergence of a superior offer – common deal protection mechanisms negotiated by the prospective acquirer at the time of initial announcement such as a pre-bid stake, exclusivity, matching rights and a break fee are all subject to structural limitations that are designed to not unduly inhibit competition for control. This allows value for target shareholders to be maximised. Superior offers can and often do emerge after a board recommended deal is publicly announced. Therefore, a prospective bidder needs to be ready to either increase its price or walk away with a consolation prize of a break fee and the profit of selling any pre-bid stake into the superior offer; and/or
- a host of shareholder activism developments following public announcement – see Lesson 4.



Lesson 4: Be prepared for shareholder activism

Shareholder activism is now a well embedded deal risk in the Australian public M&A landscape. Shareholder activism can emanate from many sources including those outlined in this Lesson 4.

Target institutional shareholder

A longstanding institutional shareholder of the target may have a fundamentally different view on value than the prospective acquirer or the target board. In a volatile market, uncertainty around a target's medium to long-term prospects means that prospective acquirers, target boards and their shareholders often have significantly divergent views on value. If an institutional shareholder strongly believes that the price being offered reflects an inadequate premium for control, they often 'put their money where their mouth is' by buying further shares on-market (up to a maximum of 20%), with a view to voting down a scheme of arrangement - being the preferred deal structure for friendly take-privates. A stake of anywhere between 15% and the maximum of 20% is often enough to defeat a scheme, having regard to typical voting turnout at scheme meetings and to the fact that any target shares held by the prospective acquirer will be excluded from voting.

Example

A recent high profile example is AustralianSuper increasing its shareholding in Origin Energy from 12.66% when the EIG/Brookfield take-private transaction was first announced to more than 17% and publicly stating its intention to vote against the scheme as it considered the price being offered did not adequately reflect the long-term value of Origin. AustralianSuper followed through with its stated intention and voted against the scheme, causing it to fail.

Industry competitor that wants to block a prospective acquirer… or partner with them!

An industry competitor may acquire (further) shares in the target on-market shortly after the public announcement of a proposed deal. Their strategy may be simply to build a sufficient stake to either block an announced deal to protect its market position or to provide a 'seat at the table' in extracting a side deal with the acquirer (without any intention to make a competing offer). Again, a stake of anywhere between 15% and a maximum of 20% is often enough.

Example 1

In 2023, Mineral Resources emerged with a 19.55% stake in Essential Metals six days before a scheduled meeting of Essential Metals' shareholders to vote on a take private, all-cash scheme proposal from IGO and Tianqi Lithium. Mineral Resources' stake was pivotal in that scheme being voted down.

Example 2

Also in 2023, Chilean-based miner SQM entered into an implementation agreement with Azure Minerals under which SQM proposed to acquire all of the shares in Azure Minerals by way of a scheme of arrangement (with a fallback takeover offer if the scheme was unsuccessful). Shortly after this was announced, Gina Rinehart muscled onto the Azure Minerals register with an ~18.4% blocking stake. Faced with this potential opposing stake, the parties negotiated a revised deal structure under which Gina Rinehart and SQM agreed to partner as joint bidders, subject to Azure Minerals shareholders agreeing to the joint bid arrangements. This is similar to what played out a few years earlier in the take-private of Zenith Energy.

Example 3

Another recent high profile example is Gina Rinehart buying shares on market in Liontown Resources, following the announcement of its recommended indicative proposal from Albemarle. This prompted Albemarle to withdraw its proposal.

Lesson 4 (continued): Be prepared for shareholder activism

Industry competitor looking to make a superior offer

An industry competitor may seek to build a sufficient stake on-market as a platform to make their own competing offer for the target.

Example

Perseus Mining has recently made a competing all-cash offer for OreCorp, off the back of Perseus Mining's acquiring a 19.9% shareholding in OreCorp by a combination of private treaty and on-market purchases. Perseus Mining acquired its 19.9% stake after OreCorp had announced that it was recommending its shareholders accept a scrip/cash offer from Toronto-listed Silvercorp Metals, in the absence of a superior offer.

Environmental activist

An environmental and socially conscious activist may attempt to exert public and/or private pressure on either the bidder or the target company to provide assurances with respect to environmental issues. These activists may go one step further and buy target shares on market after a corporate control transaction is publicly announced. Typically, their strategy is to build a sufficient stake to block an announced deal that they consider environmentally and/or socially detrimental.

Example 1

A company controlled by software mogul Mike Cannon-Brookes acquired a stake of 11.28% in AGL through derivatives. Mike Cannon-Brookes' stated intention was to vote against AGL's demerger scheme. The demerger would have split AGL into two separate companies, one being a listed coal power generation business. Cannon-Brookes publicly denounced the proposed demerger as "globally irresponsible" (as its power stations would keep burning coal into the mid 2040s), "deeply flawed" and that it "risks a terrible outcome for AGL shareholders, AGL customers, Australian taxpayers and Australia". The demerger was due to be voted on by AGL shareholders on 15 June 2022. However, two weeks before the scheduled scheme meeting, AGL abandoned the demerger once it recognised that the requisite shareholder approval would not be achieved.

Example 2

Following the announcement of the proposed acquisition of Tasmanian based salmon producer Huon Aquaculture by international meat processing company JBS under a dual track scheme of arrangement structure, Andrew Forrest's private investment vehicle Tattarang increased its stake in Huon from 7% to 18% and threatened to block the proposed schemes unless JBS gave clear commitments in relation to environmental sustainability and animal welfare standards across its global operations. In response, JBS launched a secondary takeover bid with a 50.1% minimum acceptance condition to facilitate a pathway to control of Huon if Tattarang blocked the schemes. JBS ultimately gave the environmental and sustainability commitments demanded by Tattarang who voted in favour of the schemes.

Prospective acquirers - and target boards - need to anticipate a potential activist intervention and be pragmatic and nimble in their response. They need to be prepared to either hold firm on their price and transaction terms or adapt them to secure the necessary level of shareholder support to ensure a deal succeeds.

Lesson 5: Consider deploying a dual track transaction structure

To discourage competition, respond effectively to increased shareholder activism and otherwise improve execution certainty, a prospective acquirer should consider a dual-track transaction structure.

This typically entails launching a scheme and a takeover offer concurrently, with the takeover priced slightly below the scheme and the takeover being conditional on the scheme vote failing. In this sense, the takeover offer is a 'fall back' or 'Plan B' offer structure but it is formally initiated from a market disclosure and procedural perspective at the same time as the slightly higher priced 'Plan A' scheme.

This dual track offer structure can be used where a shareholder of the target - who might emerge as an opposing shareholder and/or a competing bidder - holds a stake large enough to potentially vote down the scheme (noting that a scheme requires the approval of at least 75% of the votes cast) but where that opposing stake is not large enough to defeat a Plan B takeover with a 50% minimum acceptance condition. The dual track scheme / takeover structure means that a prospective acquirer does not lose any valuable time or momentum if its 'Plan A' scheme fails to achieve the requisite level of shareholder voting support – if that happens, the Plan B takeover bid at the slightly lower price is immediately enlivened

The dual track scheme / takeover structure has been used on a number of occasions since 2019 and was upheld as valid by the Takeovers Panel in the context of the proposed acquisition of Nitro Software by Alludo in 2023. The Panel rejected a complaint from a competing bidder (Potentia) that the dual track structure was overly complex and diminished the potential for competitive offers. The Panel noted that the structure did not preclude any third party emerging with a superior proposal (indeed, the complainant, Potentia, ended up winning the contest for control of Nitro Software with its superior competing offer). The dual track scheme / takeover structure is now commonly used by acquirers in friendly takeovers to respond effectively to increased shareholder activism and otherwise improve execution certainty.

However, this is only a viable option for acquirers who are prepared to accept the possibility of ending up with less than 100% ownership of the target. This possibility arises because if the lower priced 'Plan B' takeover is activated immediately following the failure of the 'Plan A' scheme, the acquirer may, at the conclusion of their takeover, receive an overall level of acceptances greater than 50% but well below the 90% threshold required to compulsorily acquire remaining shares that are not accepted into the offer.

Example: a dual-track scheme and takeover structure is being employed by J-Power in its take-private proposal for ASX listed Genex Power Limited (MinterEllison is advising J-Power).

A variation is a dual track scheme structure where alternative scheme proposals are considered by shareholders concurrently. It has been useful in scenarios where a shareholder of the target (who might emerge as a competing bidder or an opposing shareholder) holds a stake large enough to potentially vote down one scheme but not the parallel scheme (due to different composition of classes for the parallel scheme).

Lesson 6: Be careful with 'best and final' statements

One of the tools in the armoury of a prospective acquirer to deal with intransigent and/or activist shareholders is to increase the offer price but to declare that the increased price is 'best and final'.

This is designed to put pressure on shareholders by letting them know that there is no further scope for a price increase. Under the principle of promoting 'truth in takeovers', a prospective acquirer is legally bound by this type of last and final statement.

The only avenue to depart from it is to come within any express qualification that may be attached to the statement at the time it was made e.g. the price is 'best and final, in the absence of a competing offer'.

Prospective acquirers need to exercise caution when making a 'best and final' price statement as this can backfire by boxing them into a corner, with no room to move and causing their deal to fail.

Example 1

Contest for control of Nitro Software

The contest for control of Nitro involved two competing private equity bidders, Alludo and Potentia. Alludo had the initial ascendancy, as it had undertaken due diligence and entered into an implementation deed to acquire Nitro via a 'dual track' scheme / takeover structure at a price that was recommended by the target board. However, in the background, Potentia had amassed a 19.9% stake and continued to agitate against Alludo's proposal and seek due diligence access from Nitro.

After Potentia used its 19.9% stake to vote down the Alludo scheme, Alludo's fall-back takeover offer was enlivened. However, this failed to receive any material support from Nitro shareholders due to the possibility that Potentia could improve its offer. With its scheme proposal defeated and with a view to encouraging acceptances of its fall-back takeover offer, Alludo declared its takeover offer as 'best and final', without any qualifications. In doing so, it precluded itself from any further price increases under ASIC's truth in takeovers policy.

This proved to be a major strategic misstep by Alludo, as the following day Potentia submitted an indicative offer marginally above the Alludo 'best and final' price, compelling Nitro to open its books to Potentia. After completing its confirmatory due diligence, Potentia launched a takeover bid at a slightly higher price that was eventually recommended by the Nitro board, leaving Alludo's dual track proposal in the dust bin.

Example 2

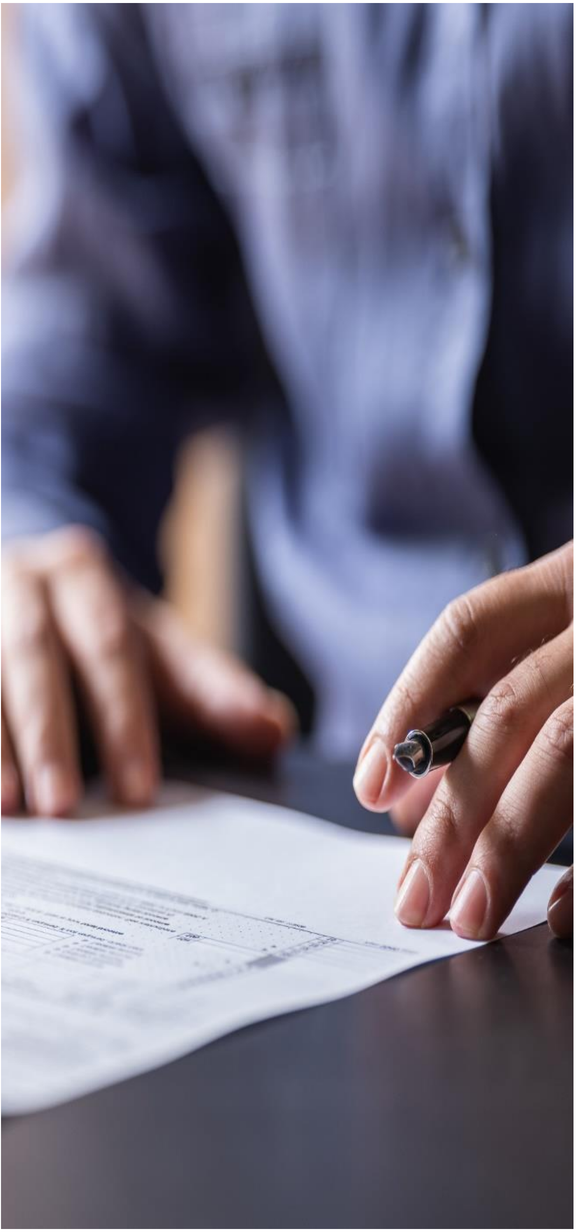
Origin Energy

Three weeks prior to the Origin Energy shareholder meeting to vote on the proposal by the Brookfield/EIG consortium to acquire all of the shares in Origin by way of a scheme of arrangement, the consortium increased its offer to a price of $9.53 per Origin share. This represented an increase of 8% on the price agreed under the implementation agreement and exceeded the top end of the independent expert's valuation range of $8.45 to $9.48 per Origin share.

The consortium's enhanced offer was made in circumstances where Origin had recently released favourable financial results and Origin's largest shareholder AustralianSuper had been publicly campaigning that the consortium's original offer did not reflect full value for Origin.

Importantly, the consortium declared that its enhanced offer was 'best and final', subject to no superior proposal emerging. The 'best and final' statement appears to have been made to pressure AustralianSuper and other shareholders to support the deal by making clear that the consortium would not further improve its offer (and would be precluded from doing so under ASIC's truth in takeovers policy, absent a superior proposal). However, within hours of the same day the consortium's enhanced offer was made, AustralianSuper announced it remained

Lesson 6 (continued): Be careful with 'last and final' statements



'substantially below' its estimate of Origin's 'long-term value' and that it remained opposed to the deal.

In the ensuing three weeks prior to the scheme meeting, AustralianSuper increased its shareholding in Origin from ~13.68% to more than 17% through on-market share purchases. At least some of the sellers of those shares may have been encouraged to sell following the consortium's 'best and final' statement, as it became apparent that the scheme was likely to fail as the consortium no longer had any legal ability to increase its offer which remained opposed by AustralianSuper who was actively building a blocking stake.

Lesson 7: Have a flexible strategy for securing your regulatory approvals

Public market deals are invariably subject to regulatory approval conditions arising from the acquirer's need to obtain one or more of FIRB clearance, ACCC clearance or similar clearances in other jurisdictions.

Depending on the industry sector, the country of origin of the prospective acquirer, and the level of competitive market overlap, these regulatory approvals can be hard and slow to obtain – or declined altogether.

The **ACCC** can take an unexpected view on market definition that is narrower or more refined than what the prospective acquirer envisaged and then require enforceable undertakings regarding partial divestiture or other mitigating steps – or at worse, oppose the acquisition altogether. FIRB is examining foreign bid proposals stringently on national interest grounds, which also encompasses national security and tax revenue protection considerations.

FIRB is also increasingly seeking additional information and granting approvals subject to conditions across data and cyber security protection, governance arrangements and tax compliance. FIRB's sensitivity is heightened if the acquirer qualifies as a 'foreign government investor'. This is a broad concept that often captures domestic and offshore private equity funds due to their upstream ownership interests with sovereign wealth funds.

In light of the complex Australian regulatory landscape, a prospective acquirer needs a flexible, well thought out strategy for securing its regulatory approvals, otherwise their deal will fail.

Example 1: ACCC

The ACCC rejected proposed acquisitions by ANZ (allowed on appeal), Transurban, Healius and Qantas, and took a lot of convincing to let deals through at Woolworths, Coles and Viva Energy. The ACCC accepted a court-enforceable undertaking from Petstock to divest a package of sites and assets, including 41 retail stores, following the ACCC's enforcement investigation into past acquisitions by Petstock. It was only on the basis of those undertakings that the ACCC did not oppose Woolworths' proposed acquisition of a 55% controlling interest in Petstock.

Example 2: FIRB

The Australian Treasurer made two prohibition orders in 2023 blocking deals involving Chinese investment into the critical minerals sector. In February 2023, the Treasurer blocked a Chinese-linked investment fund from increasing its stake in Northern Minerals Limited from 9.98% to 19.9%. Further, in July 2023, the China-linked mining company, Austroid Corporation, was prohibited from acquiring 90.10% of lithium miner Alita Resources Limited. This acquisition would have brought its stake in Alinta Resources to 100%. The Australian subsidiary of Austroid Corporation, Austroid Australia Pty Ltd, was also barred from wholly acquiring Alita Resources Limited.

Lessons for target boards

A take-private deal is arguably the most important corporate action a target board needs to navigate, with heightened reputational risks for the directors. Depending on the final outcome, their corporate reputations as stewards of shareholder capital can either be enhanced or diminished. There is little margin for error for target boards in what is a very public process after initial announcement.

We distil the key lessons for target boards, drawing on take-private deals that have either failed or were at risk of failure but ultimately succeeded.

Many of the lessons outlined above for prospective acquirers are equally relevant to target boards. Other lessons that are especially apt for target boards are discussed below.

Lesson 1: Push as much regulatory approval risk as possible onto the prospective acquirer

Public market deals are invariably subject to regulatory approval conditions arising from the acquirer's need to obtain one or more of FIRB clearance, ACCC clearance or similar clearances in other jurisdictions.

As regulatory approval conditions cannot be waived by a prospective acquirer, a target board needs to carefully evaluate these approvals including the likelihood of them being received, their likely timeframe for receipt and the capacity for a prospective acquirer to withdraw from the deal on the basis that the conditions that might be attached to those approvals are not commercially acceptable to it.

Given the uncertain timeframes associated with obtaining regulatory approvals and the possibility of conditions being imposed that may not be commercially viable to a prospective acquirer, a target board should seek to contractually allocate as much of the risks associated with those approvals as possible to the prospective acquirer. A target company can do this in three ways in the transaction agreement.

Reverse break fee

Negotiate a reverse break fee payable by the prospective acquirer to the target if the regulatory approval is declined altogether, meaning that the deal cannot complete. If commercially feasible in all of the circumstances including the degree of regulatory risk assessed by the target board, this reverse break fee should be paid by the prospective acquirer upfront, on signing. If the regulatory approval *is* received (and all other conditions are satisfied), the payment constitutes part payment of the aggregate purchase price. If the regulatory approval is *not* received, the target will already have received the break fee and does not face any payment risk. **Example:** this arrangement was deployed by the Sirtex board in 2018 when negotiating the superior offer from CDH Investments and China Grand Pharmaceuticals, which was subject to FIRB approval (this was received and the superior offer was ultimately consummated).

Obligation to accept regulatory conditions

Impose a contractual obligation on the acquirer to do whatever is needed to obtain a required approval - including agreeing to whatever conditions the relevant regulator may impose, rather than leaving it to subjective discretion of the acquirer to decide whether a condition is acceptable to it. This is colloquially referred to as a 'come hell or highwater' obligation.

More often than not, a buyer in a take-private transaction will have sufficient negotiating leverage to resist this type of 'hell or high water' obligation. A more balanced position is for the acquirer to agree to conditions that FIRB has imposed on it in prior transactions and/or to conditions which would not reasonably be expected to result in an adverse material financial impact on the value the acquirer could reasonably expect from the transaction.

'Ticking fee'

Negotiate a so-called 'ticking fee' payable by the acquirer if a required regulatory approval is not received by a specific date (which means completion cannot occur by that date). In such cases, the acquirer has to pay an extra amount for every additional day that the required regulatory approval isn’t received.

Examples: ticking fee mechanisms were included in the proposed acquisition of Origin by Brookfield/EIG and the proposed acquisition of Alliance Aviation Services by Qantas, each of which involved significant regulatory approvals (with the ACCC ultimately blocking the latter).

A similar ticking fee mechanism has been negotiated by CSR in its 'friendly' acquisition by Saint-Gobain, if completion is delayed beyond 26 June 2024.

Lesson 2: Be wary of material adverse change (MAC) conditions

Due to embedded statutory timeframes that apply to a take-private transaction in Australia, there is a long lead-time between public announcement and closing. This is at least two months but often longer if there are multiple regulatory approvals required and/or if the proposal has a complex structure which requires elevated disclosure to shareholders.

To protect the prospective acquirer's position during this lead time, it is standard for it to have the benefit of a 'no material adverse change' condition. This allows the prospective acquirer to walk away without paying a break fee or other penalty if the target suffers a material adverse change event between public announcement and closing.

Although this condition is now standard in most public market deals, a target should seek to ensure that the triggers for what constitutes a material adverse change are drafted by reference to clear, objectively ascertainable financial metrics (for example, a diminution by a specified percentage in EBITDA, consolidated net assets or consolidated revenue or a specified increase in net debt). A target should seek to avoid more general, qualitative criteria that are potentially capable of subjective interpretation and reliance by a prospective acquirer.

A target also needs to ensure that appropriate carve outs or exclusions are incorporated into the condition. That way, even if any of the triggers (financial and/or qualitative) are met, the exclusions operate to disqualify the prospective acquirer from relying on the material adverse change. These carve-outs vary considerably from deal to deal and are a key negotiation item.[v]

There have been multiple examples over the years where prospective acquirers have sought to invoke material adverse change conditions to withdraw entirely from a publicly announced deal or to renegotiate a lower price. This was especially the case with the onset of the Covid pandemic. In some cases, the acquirer succeeded. Even if the acquirer did not succeed, the purported reliance on the material adverse change condition created material delay and market instability for the target, and sometimes a reduced offer price.

Examples

Australian deals where MAC conditions were invoked in 2019/2020

Target	Acquirer	Deal structure	Value	Outcome
Pioneer Credit	Carlyle Group	Scheme	\$120 million	Terminated by target after dispute with bidder regarding MAC
Abano Healthcare	BGH Capital / OTTP	Scheme	\$129 million	Renegotiated with lower price and adjusted consideration structure
CML Group	Affinity owned Scottish Pacific Groups	Scheme	\$130 million	Terminated by mutual agreement after dispute, with bidder agreeing to contribute to target costs
Liquefied Natural Gas	LNG-9	Takeover (off-market)	\$115 million	Withdrawn due to MAC

Lesson 3: Engage with your key shareholders before going public

History has repeatedly shown that it is dangerous for a target board to publicly announce and recommend a take-private transaction without sounding out their key institutional shareholders in advance as to their view on value. Institutional shareholders typically have a long-term view on value and are not seduced by the premium that a prospective acquirer is offering 'today' – often being a point in time that deliberately coincides with share price weakness, broader market volatility or other opportunistic considerations.

With their long-term value lens, institutional shareholders typically are not persuaded by a unanimous public recommendation from a target board – especially if the board doesn't collectively have a large amount of skin in the game with their combined shareholding. Similarly, institutional shareholders often discount an independent expert's opinion that the deal is 'fair and reasonable' and in their 'best interests'.

A failure by the prospective acquirer and target board to lock-in the support of key shareholders before or at the time of public announcement, including by eliciting a public statement of voting intention, **exposes the prospective acquirer to a subsequent price negotiation behind closed doors.** This could either play out with a 'who blinks first' binary outcome – either the prospective acquirer seeks to accommodate the privately communicated price expectations of the key shareholder (and the enhanced deal then gets approved) or the prospective acquirer sticks to its original pricing and rolls the dice on the outcome of the scheme vote. If the deal fails, the target board will need to explain to shareholders why the board embarked on an expensive and time consuming process that ultimately failed, without sounding out and shoring up the key shareholder support from the outset.

Lesson 4: Beware of industry competitors who may want to scupper your deal

It's not just existing key shareholders that a target board (and prospective acquirer) need to focus on – it's also industry competitors who do not like the prospect of control of the target passing to the prospective acquirer.

There have been multiple instances over many years where an industry competitor seeks to protect their market position by purchasing target shares on market (up to 20%) between public announcement and expected deal completion, with a view to defeating the scheme vote (if the deal is structured as a scheme) or blocking compulsory acquisition (if the deal is structured as a conventional takeover), or securing a 'seat at the table' in extracting a side deal with the acquirer. Again, a stake of anywhere between 15% and a maximum of 20% is often enough.

If this risk, which cannot be eliminated, materialises, the target (and often the prospective acquirer) will be forced into a reactive position where it needs to adjourn the scheme meeting to buy time to launch a concerted shareholder engagement campaign, seeking to elicit as much shareholder support as possible before the scheme vote, with a view to overcoming the blocking stake amassed by the industry competitor. Sometimes this works. For example, Amcom Telecommunications' shareholder engagement campaign succeeded in allowing its merger with Vocus to be approved, despite TPG Telecom spending approximately $98 million to increase its stake in Amcom from 6.7% to 19.9% through on-market purchases, accompanied by a public statement by TPG that it would be voting its stake against the scheme and had no intention of making a competing offer for Amcom. But more often than not, a concerted shareholder engagement campaign is not enough to neutralise the voting impact of the industry competitor, especially if the target has a large and dispersed share register (see e.g. Origin Energy where the shareholder engagement campaign did not elicit enough support to overcome AustralianSuper increasing its stake in Origin to more than 17% and voting that stake against the EIG / Brookfield scheme.

An industry competitor may also seek to build a sufficient stake in the target on-market as a platform to:

- make their own competing offer for the target; or
- inject themselves as a co-investor (joint bidder) alongside the initially recommended acquirer (see e.g. the take-private offers for Azure Minerals and Zenith Energy).

Lesson 5: Ensure you have robust deal protection in scrip mergers

So-called 'mergers of equal' and other all scrip based mergers necessarily have a notional acquirer - which will be the continuing listed entity - and a notional target - which will become a wholly owned subsidiary of the notional acquirer and delisted from ASX. These mergers are often implemented by way of a scheme of arrangement between the notional target and its shareholders.

The target's shareholders are offered new shares in the acquirer in exchange for their shares and they will typically emerge collectively holding anywhere from 20% to greater than 50% of the notional acquirer. It is imperative that the implementation agreement for these types of transactions have reciprocal deal protections (exclusivity, break fee and matching rights) that apply equally for the notional target's benefit. Otherwise, the notional target could be left high and dry with significant sunk costs if the notional acquirer withdraws to pursue a superior proposal that it subsequently receives before the scrip merger is consummated. Typically this takes the form an all cash offer for the notional acquirer at a significant premium to its prevailing market price but conditional on it not completing its merger with the target.

Example 1

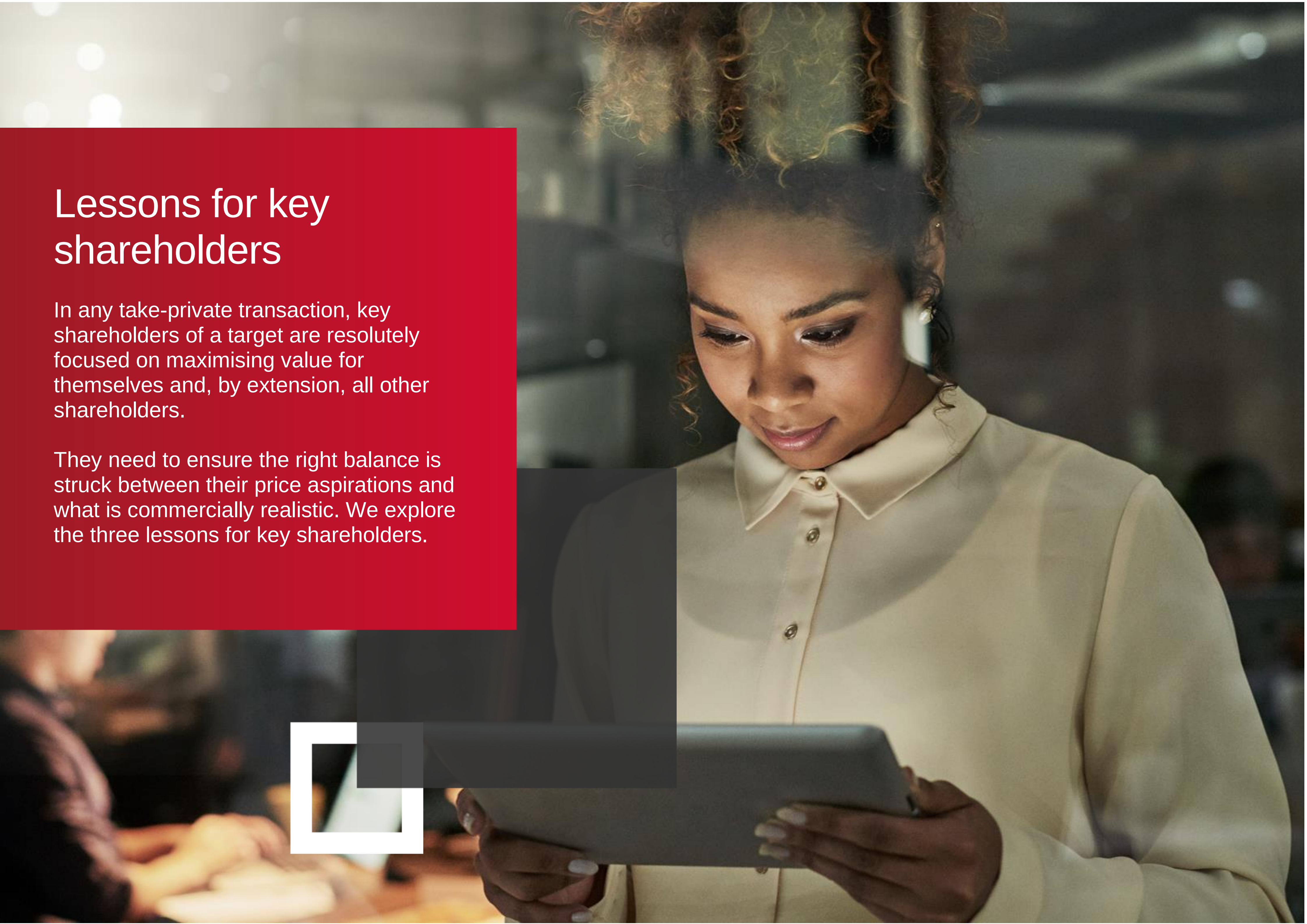
Horizon Oil learnt this painful lesson in its failed scrip merger with Roc Oil in 2014. This was to be effected by scheme of arrangement between Horizon Oil and its shareholders. Under the terms of the scheme, Horizon Oil shareholders would be offered Roc Oil shares as scheme consideration and on implementation of the scheme:

- *Horizon Oil would be a wholly owned subsidiary of Roc Oil; and*
- *the Horizon Oil shareholders would own approximately 58% of Roc Oil.*

The Horizon scheme meeting to vote on the merger with Roc Oil was cancelled and the proposed merger never proceeded. This is because three days before the scheduled scheme meeting, the notional acquirer - Roc Oil – received an all cash offer from a Hong Kong listed company, conditional on Roc Oil's merger with Horizon not proceeding. The Roc Oil board concluded that this cash offer was superior to the merger proposal with Horizon. Roc Oil terminated the implementation agreement and walked away from the deal, with no compensatory break fee payable to Horizon for its sunk costs. These were substantial including the costs of preparing the scheme booklet (which included the cost of an independent expert's report), obtaining orders from the Court to convene the scheme meeting and proceeding to convene that meeting.

Other examples

There have subsequently been other messy situations where a string of prospective acquirers have looked to potentially extricate themselves from agreed scrip based deals to pursue better offers. That was the case in the Perpetual / Pendal merger (2022), in the Gascoyne / Firefly merger (2021), and in Gloucester Coal / Yancoal merger (2009). See link here for further details [M&A brides and grooms - lessons from the altar of the NSW Supreme Court - Insight - MinterEllison]



Lessons for key shareholders

In any take-private transaction, key shareholders of a target are resolutely focused on maximising value for themselves and, by extension, all other shareholders.

They need to ensure the right balance is struck between their price aspirations and what is commercially realistic. We explore the three lessons for key shareholders.

Lesson 1: Be careful of a rose tinted, blue sky view on value

In many take-private transactions, key shareholders invariably want more money than what is being offered - i.e. a bigger premium to the market price than what the acquirer is putting on the table.

Key target shareholders should actively seek to negotiate the best price possible with a prospective acquirer, either before the deal is publicly announced (assuming they are sounded out in advance) or after the deal is publicly announced and before the shareholder vote (in the case of a scheme) or before the closing date of the offer (in the case of a takeover bid). This is especially the case noting that often a bidder's first offer is not necessarily its best and final offer.

But pushing too hard on price can be counterproductive. Using a key shareholding to defeat a scheme because you consider that the premium is inadequate can lead to significant subsequent remorse. Key shareholders sometimes need to adopt a pragmatic view on value that has due regard to the company specific and industry specific risks the target faces. The future is inherently uncertain and there have been instances where a rose tinted, blue sky view on value was applied to defeat a scheme, only for the share price performance of the target over the ensuing years to fall well behind the price that was offered. With the passage of time, the key shareholder's optimistic view on future value was proven to be spectacularly wrong.

Example

In 2011, Redflex - a global intelligent transportation systems and automated enforcement solutions company - was the subject of a failed A$303.5 million take-private offer by the Macquarie Group and Carlyle Group. The founder and key shareholder of Redflex (who was also its longstanding former chairman) used his stake to vote down the scheme, believing the offer was inadequate. Redflex continued as an ASX listed company, only to encounter a succession of operational and governance problems including executive bribery and fraud matters. Redflex was eventually privatised in 2021 for considerably less than half the value that was offered 10 years earlier.

Lesson 2: Think carefully before agreeing to publicly support an announced deal

Shareholder intention statements are an established but complex feature of public M&A transactions. They play an important role in both 'friendly' and 'hostile' takeovers bids by providing a public indication of the level of shareholder support (or opposition) for an announced control transaction. For different reasons, this may be important to both the prospective acquirer and the target.

For a prospective acquirer, a positive intention statement from one or more key shareholders can provide important public support and momentum for a takeover bid to succeed. It may also have a 'chilling' or 'deterrent' effect on potential rival bidders (although this potential effect is largely attenuated if a shareholder intention statement is appropriately qualified as applying 'in the absence of a superior proposal').

For a target, a positive intention statement from one or more key shareholders may provide a valuable insight into as to whether or not a 'friendly' control proposal will succeed, especially in the context of a scheme of arrangement where the target will bear the majority of the costs in proposing and implementing the scheme.

In December 2015, the Takeovers Panel issued a guidance note on shareholder intention statements to clarify the permissible boundaries for these statements. This guidance is helpful. A number of principles are now clear and can be stated with certainty. Other important points, however, remain unclear and can create uncertainty for bidders and targets, as well as substantial shareholders who may be approached to provide a shareholder intention statement. Bidders, targets and substantial shareholders who are approached to provide public intention statements all need to exercise caution and judgment in this fluid and unsettled area. Please see Shareholder intention statements in takeovers - navigating the uncertainties - Insight - MinterEllison for a summary of what is now clear and what remains unclear, together with some practical guidelines for bidders, targets and substantial shareholders respectively.

Lesson 3: If you don't like a scheme and want to vote it down, you don't need 20% (something less will often suffice)

As noted above, institutional shareholders and/or industry competitors who are opposed to a proposed scheme often take the step of buying (further) shares in the target on-market, in the period after the scheme is publicly announced and before the scheduled scheme meeting.

This has proven to be an effective strategy to build a sufficient voting stake to defeat a proposed scheme and/or to use the stake as the launching pad for making a competing offer for the target. The maximum stake that an opposing institutional shareholder and/or industry competitor can lawfully acquire is 20% - anything above this threshold needs to be by way of a takeover offer or through some other recognised exception to the so-called 20% prohibition.

In practical terms though, it is often not necessary for an opposing institutional shareholder and/or industry competitor to buy up to the 20% maximum. Often a stake comfortably under 20% will be sufficient to defeat a scheme vote, especially if the target has a widely dispersed share register. The reason for this is that although the voting threshold for a scheme to fail is 25.01%, this is assessed only by reference to shareholders who actually attend and vote at the scheme meeting, whether in person, by proxy or (in the case of a corporate shareholder) by corporate representative. Historically, voter turnout at scheme meetings is only around 65% of the total shares on issue. Therefore, an opposing stake of, say, 17% is magnified for scheme voting purposes and is often enough by itself to cause a scheme vote to fail.

Not buying up to the full permitted limit of 20% can deliver a material economic saving for an opposing shareholder, both in terms of a lower overall financial outlay and then containing the subsequent paper loss on the acquired stake. The opposing shareholder will, if they are successful in defeating the scheme, incur a substantial paper loss on its investment in the scheme company. They will have purchased shares on-market at a price significantly above the pre-announcement price. If the opposing shareholder uses its stake to vote down the scheme, the price of the target's shares will (all other things being equal) fall to pre-announcement levels, meaning that the opposing shareholder will incur a significant paper loss on its investment, even though it may have achieved its aim of defeating the scheme. If the opposing shareholder is itself listed, that paper loss on its investment (as well as the financial outlay to acquire the stake itself and what to do with that stake going forward) may have an adverse impact on its own share price.

Conclusion

For prospective acquirers, target boards and key shareholders of the target, a take-private deal is rarely straight-forward. In the period from initial public announcement to expected completion, there are invariably challenges for all three stakeholders groups to navigate.

As this publication shows, a take-private deal can quickly move from promise to peril. All three stakeholder groups need to be mindful of the common downfalls that have afflicted past deals. Having a flexible, pragmatic approach, with contingency arrangements to respond to these potential downfalls, is paramount.

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Endnotes

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[i] MinterEllison's research discloses that of the 132 formal, binding take-private proposals announced in the two year period between 1 January 2022 to 31 December 2023, only 20 were unsuccessful or withdrawn. The reasons include those captured by the lessons in this article. Note: these statistics and this publication do not cover unsuccessful or withdrawn non-binding indicative proposals. These preliminary proposals are often disclosed to the market (either voluntarily or in response to media coverage) and have a much higher failure rate, as they are subject to due diligence and negotiation of price and other terms. A recent, high profile example of an unsuccessful or withdrawn non-binding indicative proposal is that in relation to the proposed merger of Santos and Woodside.

[ii] The year reflects the date the binding transaction was publicly announced by the target.

[iii] Dye & Durham was not prepared to proceed without a price reduction given that UK FCA approval was conditional on Link Group setting aside $518 million to cover potential fines. In December 2023, Mitsubishi UFJ Financial Group has agreed to acquire Link Group for $1.2 billion via scheme of arrangement (down from $2.5 billion from Dye & Durham).

[iv] In response, Symbion devised an alternative two-tiered proposal involving the sale of specific assets to Healthscope, to be followed by a scheme of arrangement under which a private equity consortium would acquire Symbion. This alternative proposal was withdrawn prior to the Symbion shareholder vote on the first element due to the non-receipt of an ATO ruling sought by Symbion regarding the availability of capital gains tax rollover relief and demerger relief. Prior to the alternative proposal being withdrawn, Primary made an all cash Ch 6 takeover bid for Symbion. This bid was initially rejected by the board of Symbion but ultimately recommended, with Primary succeeding in acquiring 100% control of Symbion.

[v] Typical carve outs include matters that were fairly disclosed to the prospective acquirer prior to entry into the contract, matters capable of ascertainment from publicly available searches before entry into the contract and matters which relate to macroeconomic, geopolitical or similar external events that are not specific to the target's business e.g. Covid-19 pandemic. This last carve out is directed at capturing the principle that the purpose of a 'no material adverse change' condition is to protect a prospective acquirer against problems *in the subject business*, not broader events unfolding in the industry or world at large generally that have impacted the target (and other participants in the target's industry).

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