

This paper¹ recommends the introduction of a mandatory² disclosure regime for prospective information³ in takeover documents⁴ together with a stand-alone, safe-harbour defence⁵ for participants⁶ that have acted honestly and in good faith.

Prospective information is considered by many to be inherently dangerous⁷ and potentially misleading.⁹ However, in certain circumstances this type of information is a useful¹⁰ and relevant form of information in assisting shareholder or investor decisions in a takeover.¹¹ As this information is prepared on the basis of various assumptions of future events and conditions reasonably expected to occur, it can potentially mislead. The current tensions¹² pertaining to the disclosure of prospective information needs to change to create a more transparent market. Shareholders and retail investors need complete access to a range of prospective information to allow a more informed decision to occur independently.

¹ Alan D'Andrea Paper - Masters of Law – Company Takeovers LAW70042 (Co-ordinator Mr Rodd Levy)

² It is not mandatory for product issuers in takeovers and prospectus offers to disclose prospective information. Silence may constitute misleading or deceptive conduct see *Demagogue Pty Ltd v Ramensky* (1992) 39 FCR 31 judgment of Black CJ.

³ Prospective includes references to future events and forward looking statements. Also see Australian Securities and Investments Commission (ASIC) Regulatory Guide 170 Prospective financial Information (RG 170) states that prospective information includes information, for example, forecasts and projections of future performance, benefits or costs. It may also be presented in different ways, such as numerically or using charts or graphs.

⁴ In particular, off-market takeovers where the bidder issues new shares as consideration for the purchase price of the target. See section 636(1)(g) of the Corporations Act provides "if the bid price includes the issue of securities of the bidder or parent of the bidder, then the Bidder's Statement must also contain all the information that would be required in a prospectus for a public offer of those securities". The general disclosure obligations of a bidder in a takeover are set out in section 636 of the Corporations Act.

⁵ Apart from due diligence defences available under Section 731 of the Corporations Act. Due diligence defences require management to show they have put in place an effective internal control or compliance system. In some instances a court will request that the scheme directors confirm within the proposed scheme that it has been subject to adequate due diligence (see *Re Adelaide Bank Limited* [2007] FCA 1582). See Tatiana Stack 'Mergers & Acquisition Structuring' (2011) 8 *Macquarie Journal of Business Law* 243, 245.

⁶ Participants or takeover participants refer to bidders, targets, its directors, officers and advisors unless specifically stated otherwise.

⁷ ASIC RG 170.3 and academic articles here

⁸ See Jason Kyrwood, 'Disclosure of forecasts in prospectuses' (1998) 16 *Company and Securities Law Journal* 352.

⁹ See Gill North, 'Companies take heed: The misleading or deceptive conduct provisions are gaining prominence' (2012) 30 *Company and Securities Law Journal* 342, 351.

¹⁰ Above n 8, 352 to 354.

¹¹ Tony Damian and Andrew Rich, *Schemes, Takeovers and Himalayan Peaks* (The University of Sydney, 3rd Edition, 2013) 23.

¹² Further, the takeover regulations are based on the Eggleston Committee's four principles, which are designed to ensure that the proposed takeover is in the best interest of the target shareholders as the owners of the company. The four Eggleston principles benefit the target shareholders as they ensure the following is provided: the identity of the party seeking control; a reasonable amount of information on which to base their offer; a reasonable amount of time to consider the offer; and, as far as possible, an equal opportunity for all shareholders to benefit from the bid

This paper considers the current disclosure laws and dangers surrounding the disclosure of prospective information. Recent ASIC litigation against ASX listed companies and class action settlements together with ASIC research¹³ and guidance papers¹⁴ in the area are reviewed. It advocates the introduction of a mandatory disclosure regime for prospective information in takeovers and that a stand-alone defence be available for takeover participants that have acted honestly and in good faith.¹⁵ Disclosure documents¹⁶ in change-of-control transactions¹⁷ should contain prospective information to provide a range of potential outcomes of the future operations of the parties.

It suggests reform is required to reduce the flexibility and discretion currently available in the release of prospective financial information in takeovers.¹⁸ A mandatory disclosure regime would increase the range of information currently provided to shareholders and detail a range of potential outcomes arising from the proposed transaction. This reform would also see the introduction of a clearly defined format, financial ratios and terms including net profit after tax, statutory profit and the re-introduction of financial forecasts and financial projections.¹⁹ This would enhance efficiency, innovation and certainty for regulators, issuers and investors.

The perceived problem arises from whether shareholders and retail investors are assisted by the disclosure of prospective information. Those supporting mandatory disclosure, including this author, argue that retail clients must be provided and have access to a range of prospective information that provides a sensitivity analysis of the proposed transaction.

¹³ Australian Securities and Investments Commission (ASIC), "ASIC's Review of 30 June 2010 Financial Reports and Focuses for 31 December 2010" (22 December 2010) Media Release 10-282AD (ASIC 2010 Review); ASIC, "Improved Financial Information for Investors and Others" (21 December 2011) Media Release 11-312MR (ASIC 2011 Review); North, Gil, "Continuous Disclosure: The Empirical Uncertainties" (2011) 29 *Company and Securities Law Journal* 394.

¹⁴ ASIC, Regulatory Guide 228, Prospectuses: Effective Disclosure for Retail Investors (Nov 2011) (ASIC, RG 228); ASIC, Regulatory Guide 230, Disclosing Non-IFRS Financial Information (Dec 2011) (ASIC, RG 230).

¹⁵ See the power of Courts to grant relief from liability under section 1318. *Australian Securities and Investments Commission v Healey (No 2)* (2011) 196 FCR 430 at [132]-[142].

¹⁶ Takeover documents include bidder statements, target statements and market presentations.

¹⁷ The term change-of-control is used interchangeably with the term mergers and acquisitions or ('M&A'). These terms are used to cover many corporate transactions, including takeovers, schemes of arrangement, divestitures, spin-offs, privatisations and leveraged buyouts. For a broad description of some of these activities, see Greenhill & Co Inc, Form S-1 Registration Statement filed with the Securities and Exchange Commission on 11 March 2004, pp 44- 45 (www.sec.gov).

¹⁸ The proposed reform to prospective information disclosure requirements in a takeover shall also extend to prospectus offers thereby enhancing certainty and uniformity in the financial product issuer market.

¹⁹ See ASIC Practice Note 67 Financial Forecasts in prospectuses

This type of prospective information has the potential to empower users to arrive at a better informed decision through independent analysis. Disclosure of all future plans and potential outcomes of a proposed takeover are crucial in the decision-making process especially when accepting bidder's shares as consideration.²⁰

ASIC has not gone far enough in encouraging the disclosure of prospective information in takeovers or clarified the obligations of parties in takeovers under existing legislation to include prospective information. A safe harbour to takeover participants in relation to disclosure of prospective information should be made available. This reform to takeover disclosure will improve the quality of information disclosed to target shareholders, and provide certainty for bidders and targets while encouraging entrepreneurial risk and ensure director liability is limited.

This paper commences by examining the policy underpinnings ASIC views on the disclosure of prospective information including takeovers, existing laws to disclose forecasts in takeovers and recent judgements in the area. It concludes that there is a case for the adoption of a mandatory disclosure regime for prospective information given the current quality and quantity of disclosure in the area.

Introduction

Change-of-control transactions play a significant role in driving growth, efficiency and innovation in the financial markets. The availability and quality of prospective information within takeover disclosure documents needs to continue to improve for Australia financial markets to flourish. Current industry best practice²¹ utilises specialist advisers²² that tend to boilerplate and overly desensitize this information which is then displayed in confusing formats.

Prospective information is considered to be a useful and relevant form of information to many.²³ Issuers should not have the discretion as to its disclosure in takeovers.²⁴ However, corporate

²⁰ B Mann, 'Prospectuses: Unreadable or Just Unread? – A Proposal to Re-examine Policies Against Permitting Projections' (1971) *George Washington Law Review* 222.

²¹ D'Andrea, Alan, *A Practical Guide to Listing on the ASX (GORG Publishing, 4th edition 2012)* 16.

²² Valuation experts in most instances a specialist firms that purely focus on the area of prospective information. (e.g. Greenhill) See ASIC Regulatory Guide 111 Content of expert reports and ASIC Regulatory Guide 112 Independence of experts.

²³ Above n 8, 354.

²⁴ ASIC RG170.9. Please see the balancing act between relevance and reliability that issuers currently need to undertake.

legislation already imposes a wide range of various disclosure obligations that are periodic, ongoing, general and specific.²⁵ The level of disclosure depends on type, complexity and size of the corporation. Private, public²⁶ or publicly listed company on the ASX²⁷ have similar, but not the same, disclosure requirements.²⁸ Directors, officers²⁹ and advisers³⁰ are subject to a broad range of liability³¹ laws for incomplete and inadequate disclosure that impose severe penalties, especially in the case of misleading³² and deceptive conduct.³³

This paper supports the introduction of a mandatory disclosure regime for prospective information for takeovers in Australia. In addition, takeover participants including directors³⁴, officers,³⁵ advisers³⁶ that act honestly and in good faith³⁷ should have available a stand-alone defence (for example, a statutory safe harbour) for the disclosure of prospective information.

This proposed reform supports the direction outlined in ASIC guidance papers recently released³⁸ in the area to enhance the quality and level of disclosure currently being made available to retail investors. ASIC's concerns with this area has seen the release of a number of Regulatory

²⁵ Financial Services Reform Act 2001 (Cth) (FSRA).

²⁶ See the Corporations Act 2001 (Cth), Chapter 2M. Small proprietary companies are not generally subject to these requirements sections 292-294.

²⁷ ASX Listed entities are subject to a range of mandatory disclosure obligations under the Corporations Act.

²⁸ See ASX Listing Rules available at www.asx.com.au

²⁹ The term 'officer' is defined by section 9 of the Corporations Act and includes a director or secretary or a person who makes, or participates in making, decisions that affect the whole, or a substantial part, of the business of the corporation or who has the capacity to affect significantly the corporation's financial standing.

³⁰ Andrew Tuch, 'Obligations of financial advisers in change-of-control transactions: Fiduciary and other questions' (2006) 24 *Company and Securities Law Journal* 488 the inconsistent standards imposed on financial advisers to avoid conflicts and the statutory obligation under the Corporations Act 2001 (Cth).

³¹ Section 670A, 728, 953A and 1022A of the Corporations Act prohibit misstatements or misleading or deceptive disclosure within a range of documents including compulsory acquisition and buy-out documents, fundraising documents, financial services guides, statements of advice and product disclosure statements.

³² ASIC RG 228.100 highlights that the use of warnings and other cautionary language will not always be sufficient to prevent particular information being misleading

³³ See *Centro* case.

³⁴ Directors include executive directors and non-executive directors. Section 180(1) of the Corporations Act provides that directors and other officers of a corporation must exercise their powers and discharge their duties with the degree of care and diligence that a reasonable person would exercise if they: were a director or officer of a corporation in the corporation's circumstances; and occupied the office held by, and had the same responsibilities within the corporation as, the director or officer.

³⁵ See *James Hardie* case discussed below.

³⁶ Should a due diligence defence be available independent experts that provides specialist reports such as valuations, investigating accountant's report (IAR) as well as to investment bankers that provide financial advisory services to company involved in change-of-control transactions; Tuch, above n13, 490.

³⁷ What constitutes acting honestly and in good faith was discussed in *Australian Securities and Investments Commission v Healey (No 2)* (2011) 196 FCR 430 at [132]-[142]; Robert Baxt, '*The James Hardie decision – the penalty decision: honesty is apparently the best policy!*' (2009) 5 *The Baxt Report* 1.

³⁸ In 2010 and 2011.

Guides³⁹ and consultation papers in an effort to improve disclosure to retail investors so that it is clear, concise and effective.⁴⁰ There have been a number of cases regarding prospective information in takeover documents,⁴¹ as well as ASIC actions⁴² regarding inadequate prospectus forecast disclosures.⁴³

What is Prospective information?

Prior to considering legal requirement for the disclosure prospective information in a takeover this papers examines the types, usefulness and accuracy of prospective information. ASIC guidance papers and recent decisions regarding prospective information, in particular financial forecasts are also examined.

Prospective information by virtue of its forward-looking character is inherently dangerous⁴⁴ and considered to be potential unreliable⁴⁵ and not relevant.⁴⁶ Information is said not to be material if it is 'speculative or based on mere matters of opinion or judgment.'⁴⁷ Prospective information is sometimes referred to as soft⁴⁸ information⁴⁹ but this does not mean it is not useful.⁵⁰ Soft information is a term that derives from the United States and refers to

³⁹ See ASIC Regulatory Guide 228 – Prospectuses: Effective disclosure for retail investors, ASIC Regulatory Guide 170 Prospective financial information [RG 170] and ASIC Consultation Paper 150 Disclosing financial information other than in accordance with accounting standards [CP 150].

⁴⁰ Takeover Panel's decision in Northern Energy Corporation Limited [2011] ATP 2 at paragraphs 111–112.

⁴¹ For the purposes of this paper takeover documents refers to a prospectus and/or bidder's statements and target statement see section 670 of the Corporations Act.

⁴² See iSelect prospectus forecasts action – discussed below.

<http://www.smh.com.au/business/asic-demands-company-files-in-probe-of-iselect-float-flop-20130915-2tsro.html> (visited 16 Jan 2014).

⁴⁴ See ASIC RG 170.3. Also see *Solomon Pacific Resources NL v Acacia Resources Ltd* (1996) 14 ACLC 505. In *Solomon*, the court held: Predictions, whether in the form of forecasts or projections or in any other form, are inherently speculative and subject to contingencies of varying degrees of probability and foreseeability. The very inclusion in a Pt A statement of such a prediction may well be potentially misleading.

⁴⁵ ASIC RG 170.9 and 170.11

⁴⁶ ASIC RG 170.11

⁴⁷ See ASIC RG 170.11 and *AAPT v. Cable & Wireless Optus Ltd* (1999) 32 ACSR 63.

⁴⁸ Schneider, C "Nits, Grits and Soft Information in SEC Filings" (1972) 121 *University of Pennsylvania Law Review* 254.

⁴⁹ Hard information has been defined as statements concerning objectively verifiable historical events or situations: *ibid* at 255. In the United States, Pastena and Ronen found company managers disclosed information as if they attempted "to delay the dissemination of negative information, relative to positive information", disclosed primarily soft positive information rather than soft negative information, and disclosed negative information only after such information became hard. (see *Pastena V and Ronen J, "Some Hypotheses on the Pattern of Management's Informal Disclosures"* (1979) 17 *Journal of Accounting Research* 550 at 563-564.

⁵⁰ ASIC RG 228.100, Also see Information is useful if it assists investors in determining how to allocate their scarce resources. Above n 8, 352.

information that is subjective in nature.⁵¹ It is clear from the case law and ASIC⁵² that the factors to be taken into consideration in assessing whether soft information is material or reasonably required, remains largely unsettled.⁵³

Prospective information involves subjective evaluations, opinions or estimates that do not lend themselves well to objective verification.⁵⁴ Even Regulators and industry commentators have highlighted that all financial information historical or prospective (forward looking) is subject to personal views and uncertainty⁵⁵ due to approximation.⁵⁶

ASIC provides that it is the issuer's decision to determine whether or not to include prospective financial information in a disclosure document. This decision requires balancing the information value (relevance) of what is disclosed against the likelihood that the information may be misleading (reliability).⁵⁷

A disclosure document should include prospective information if there are reasonable grounds for it being included.⁵⁸ 'Reasonable grounds' means that there must be a sufficient objective foundation for the statement. The factors that may amount to reasonable grounds include information that is underpinned by independent industry experts' reports or independent accountants' reports.⁵⁹ However, ASIC further provides that information supported only by hypothetical assumptions do not, by themselves, indicate reasonable grounds⁶⁰ but statements based on a contingency that is unlikely to occur are not prohibited. ASIC acknowledged that in many cases these statement will have a predictive faculty and this decision needs to be determined by the issuer. Rather than pretending that subjectiveness has no part to play ASIC should support the re-introduction of financial forecasts and projections into disclosure documents. An issuer can avoid providing

⁵¹ Craig Callum and Larelle Law, 'Soft information disclosure requirements under the Corporations Law' (2001) 29 *Australian Business Law Review Journal* 149.

⁵² See ASIC RG 170.25.

⁵³ See contrasting decisions in *Pancontinental Mining Ltd v Goldfields Ltd* and *Solomon Pacific Resources NL v Acacia Resources Ltd*, which failed to provide a definitive answer.

⁵⁴ Above n 8, 351.

⁵⁵ *Hunt Contracting Co Pty Ltd v Roebuck Resources NL (Hunt Contracting)* [1992] ATPR 41-193 at 40,617.

⁵⁶ Above n 8, 352. Also referenced at R Barondes, 'The Bespeaks Caution Doctrine: Revisiting the Application of Federal Securities Law to Opinions and Estimates' (1994) 19 *Journal of Corporation Law* 243 at footnote 1.

⁵⁷ See ASIC RG 170.9

⁵⁸ See ASIC Rg 170.16

⁵⁹ See ASIC RG 170.25-170.41

⁶⁰ The test in s728(2) requires that the grounds for prospective financial information be objectively reasonable.

prospective information by merely purporting to say that the future is too uncertain and there are no reasonable grounds for there to be an objective foundation for the forecast to be included. When this arises the disclosure document remains silent on the future plans of the issuer.

The disclosure of historical information has been the domain of financial accountants and auditors for centuries but still requires subjective judgment to occur. For example, to what degree should doubtful debts provisions be determined? What appears to be irrefutable fact has seen confusion in the classification and recording of simple accounting transaction that has resulted in unreliable and misleading disclosure.⁶¹ Historical information can be said to be reasonably objective and non-actionable but even then issues of judgment and opinion have found to be wanting with a number of notable exceptions.⁶²

Regulators⁶³ previously categorised prospective financial information through the use of terms such as **financial forecast** and **financial projection**.⁶⁴ The Australian Securities Commission, as it then was,⁶⁵ initially attempted to encourage prospective financial information to be disclosed by allowing and differentiating prospective financial information on the basis of the types of assumptions adopted. In *Pancontinental*⁶⁶ case, the court held that the target company and its shareholders are entitled under the law to the benefits of the disclosure in a takeover document of earnings forecasts even though they would be based on a number of assumptions and that these should be spelt out.⁶⁷

This encouragement by ASIC to allow the release of a range a prospective information has now ceased with the introduction of RG170. ASIC provides that the general test of whether

⁶¹ The Federal Court approved a settlement amounting to \$200 million, including costs, arising from the inadequate disclosure of matters in relation to Centro group entities Australian Securities and Investments Commission (ASIC) v Healey (No 2) (2011) 196 FCR 430 (Centro Case). PWC audit partners became confused as to what constituted a short term liability versus a long term liability. Also see Enron financial audit that resulted in the demise of Arthur Anderson.

⁶² Andrew McRobert and Ronnie Hoffman, *Financial Literacy: Lessons from Centro* (Thomson, 2011) 3-7

⁶³ On 4th August 1997, the Australian Securities Commission (ASC) (as it then was) released guidance for forecasts in prospectuses that are contained in Practice Note 67, *Financial Forecasts in Prospectuses* (PN67).

⁶⁴ See ASIC Regulatory Guide 146. Since March 2004 the Corporations Act 2001 requires all persons delivering a 'financial service' to hold an Australian Financial Services License ('AFSL').

⁶⁵ See ASC PN67.8 and Auditing Standard 804 issued by the Australian Accounting Research Foundation on behalf of the Institute of Chartered Accountants and Australian Society of Certified Practising Accountants, makes a distinction between a forecast and a projection.

⁶⁶ *Pancontinental Mining Ltd v Goldfields Ltd* (1995) 13 ACLC 577. This is contrast to the comments in Solomn.

⁶⁷ Stephen Walker, Richard Kriedemann, *'Forecasts: misleading or essential?'* (1997)15 *Company and Securities Law Journal* 47.

prospective financial information must be disclosed is whether it is relevant to its audience and reliable.⁶⁸ ASIC's approach is for the issuer to undertake a balancing act between relevance and reliability and make a decision as to whether disclosure of prospective information is required.⁶⁹

A *financial forecast* in a disclosure document existed if the information was prepared on the basis of **best-estimate assumptions** as to future events, future conditions and future actions to be taken by management.⁷⁰ Whereas, in the event these assumptions are merely hypothetical⁷¹ (that is, management does not necessarily expect them to take place) then the financial information was regarded as a mere *projection*⁷² that was seen as unlikely to occur. This regime came to an end when regulators found that retail investors could not distinguish the difference between a more robust financial forecast and a financial projection.

The purpose of a disclosure document is to help retail investors assess the risks and returns of an offer and to make an informed investment decision. Prospective financial information whether it be in the form of a forecast or a projection that is prepared by takeover participants should provide retail investors with highly relevant and useful information of the potential future financial performance. This information should be based upon economic, legal, operating, development and trading assumptions about future events and actions that have not yet occurred and may not necessarily occur.

A more important consideration is not the accuracy of prospective financial information; rather the accuracy of investor's predictions with and without the availability of published prospective information.⁷³ ASIC believes information is not material to investors if it is 'speculative or based on mere matters of opinion or judgment'.⁷⁴ Matters of opinion or

⁶⁸ See ASIC RG 170.11. There must be a reasonable basis for it: see GIO Australia Holdings Ltd v. AMP Insurance Investment Holdings Pty Ltd (1998) 29 ACSR 584

⁶⁹ See ASIC RG170.9

⁷⁰ See ASC PN67.7 and PN67.10.

⁷¹ See ASC PN 67.9.

⁷² See ASC PN 67.5 the distinction between forecasts and projections are illustrated and should disclose: (a) the assumptions used; (b) the extent of enquiries and research undertaken by the expert and any other compiler of the projection or forecast; (c) the specific period to which it relates; and (d) an explanation for the choice of the period covered by the forecast.

⁷³ Above n 8, 352.

⁷⁴ see AAPT v. Cable & Wireless Optus Ltd (1999) 32 ACSR 63.

judgment shall always be intertwined when prospective information is involved. The provision of prospective information based on reasonable grounds shall itself be a subjective decision to at least some degree. It is argued that takeover participants should be entitled to provide prospective information to investors both on a reasonable and hypothetical basis. This would allow them to make their own comparisons and draw their own conclusions. The speed of change in modern business practices gives rise to the need of the disclosure of a range of prospective information in takeover documents. There is currently a major liability disincentive to provide prospective information in takeovers.

Prospective Information Litigation and ASIC Action

In Australia, there are a number of cases that resulted from takeovers due to the lack⁷⁵ of disclosure of prospective information or inadequate misleading disclosure of prospective information. These cases illustrate the need for reform and the introduction of a mandatory disclosure regime of prospective information.

Solomon Pacific Resources NL (Solpac) involved an offer proposed to be made by Acacia Resources Ltd (Acacia) to shareholders in Solomon Pacific Resources NL (Solpac) for the acquisition by Acacia of all their shares in Solpac in consideration for the allotment and issue to them of one share in Acacia for every six shares in Solpac.⁷⁶ Solpac sought a court injunction to restrain Acacia from despatching the offer and other relief on the basis that the Part A Statement⁷⁷ provided no information in the nature of earnings, forecasts or cash flow projections for Acacia. Solpac claimed that information as to projections was necessary in order to enable Solpac shareholders to assess the financial prospects of Acacia and was therefore information material to the making of a decision by an offeree on whether or not to accept the offer. McLelland CJ considered that the inclusion of predictions (as distinct from facts) in the statement might be potentially misleading and was not prepared to grant an injunction on the basis of that omission of this prospective information.

⁷⁵ Solomon Pacific Resources NL v Acacia Resources Ltd (1996) 14 ACLC 505.

⁷⁶ See Armour John, 'Accounting for acquisitions in extractive industries – goodwill by another name' (1996) 14 *Company and Securities Law Journal* 485, 164

⁷⁷ Bidder's Statement under the current law.

The AMP takeover bid of GIO⁷⁸ resulted in a number of legal proceedings occurring. ASIC action against the directors of GIO arose from the target's statement profit forecast of \$250 million, of which \$80 million was at risk due to a number of natural disasters that had occurred in North America. The GIO Board recommended that shareholders reject the takeover offer by AMP, claiming that the shares were worth more. This recommendation was subsequently relied upon by former GIO shareholders who did not accept AMP's takeover offer due to their reliance on the announcements and recommendations made during the bid and commenced a class action against GIO, its former board of directors and its advisors.⁷⁹ The parties ultimately settled with a payment of \$112 million to former GIO shareholders.⁸⁰

The recent iSelect Limited matter involved its initial public offering and listing on the ASX in 2013 and August 29 announcement that its revenue of \$118 million was 2.9 per cent below prospectus forecasts of \$121.6 million. ASIC issued a Notice Requiring the Production of Books to iSelect Limited to produce all documents relating to the August 29 announcement, including "due diligence files, working papers, boardroom papers, letters, emails, facsimiles, file notes or diary entries" as well as their management accounts and board reports, together with any documents relating to management discussions of the company's revenue shortfall. Under section 674⁸¹ of the Corporation Act, it is required that listed companies tell the market of 'information that a reasonable person would expect, if it were generally available, to have a material effect' on its share price.⁸²

In this instance, if iSelect had the opportunity to provide projections in addition to forecasts this would inform retail investors that there is potential range of financial results depending on whether the assumptions of future events expected did actually occur. Allowing both forecasts and projections to be disclosed would provide a form of sensitivity analysis to be disclosed. This type of analysis is typically undertaken by professional and institutional investors as a matter of best practice. Then investors in the initial public offering would have

⁷⁸ Applicable at the time of the AMP-GIO takeover, the then takeover procedure used the terms "Part A statement" for the bidder's statement and "Part B statement" for the target's statement.

⁷⁹ Grant Samuel, *Macquarie Bank and PricewaterhouseCoopers* - after following the recommendation of directors to reject a \$3 billion takeover bid by AMP.

⁸⁰ *King v AG Australia Holdings Ltd* [2003] FCA 980.

⁸¹ See continuous disclosure obligations and AX listing rules.

⁸² See ASIC RG170.4. Contravening the section can be a criminal offence.

been better informed. Introducing a mandatory disclosure regime for prospective information would allow investors in iSelect with the opportunity to base their decision to invest in the initial public offering. Why should an issuer acting in good faith that have financial forecasts be subject to liability because it failed to meet forecasts by 2.9%.

In 2008, Aristocrat Leisure paid \$144.5 million to settle shareholder claims made through a class action.⁸³ The shareholders sought damages for investor losses resulting from alleged misleading or deceptive conduct and a breach of the continuous disclosure obligations by the company in relation to a series of profit forecasts provided to the market.

Disclosure Requirements – Takeovers

The main source of regulation of takeovers in Australia is contained in Chapter 6 of the Corporations Act. It contains the central prohibitions⁸⁴ and restrictions⁸⁵ concerning acquisitions of shares, permitted forms of takeover bids and details the information and timing that must be delivered to shareholders, regulators, exchanges and other parties in connection with a takeover bid.

Corporate legislation imposes a range of disclosure requirements that are periodic, ongoing, general and specific⁸⁶ depending on the type, complexity, listing status and size.⁸⁷ A company performing a takeover has additional general and specific disclosure requirements.

An *offeror* in a takeover is required to provide information to enable the shareholders in the target company to form a judgment on the merits of the proposal.⁸⁸ This includes the future intentions of the target business, any major changes and future employment.^{89 90}

Disclosure Obligations - Takeovers

⁸³ Dorajay Pty Ltd v Aristocrat Leisure Ltd (2008) 67 ACSR 569; [2008] FCA 1311; Dorajay Pty Ltd v Aristocrat Leisure Ltd [2009] FCA 19.

⁸⁴ Corporations Act section 606.

⁸⁵ Corporations Act section 611.

⁸⁶ Financial Services Reform Act 2001 (Cth) (FSRA).

⁸⁷ See ASX Listing Rules available at www.asx.com.au

⁸⁸ Kent, Wayne, 'Implications for disclosure in takeover documents after the ICAL and Cumberland credit decisions' (1988) 6 Company and Securities Law Journal 282.

⁸⁹ Kent, Wayne, 'Implications for disclosure in takeover documents after the ICAL and Cumberland credit decisions' (1988) 6 Company and Securities Law Journal 283.

⁹⁰ Damian and Rich, above n 11, 721-727 for detailed analysis.

The disclosure obligations of a bidder in a takeover are set out in section 636. A bidder's statement requires all information that is material to target members.⁹¹ Takeover disclosure obligations are encapsulated within the disclosure principles in section 602, colloquially referred to as the 'Eggleston principles'⁹² and the disclosure obligations in section 636 of the Corporations Act.⁹³

At the heart of the disclosure requirements for takeovers is the concept of materiality⁹⁴ in that any information that has the capacity to influence a party's decision⁹⁵ and judgment to decide one way rather than the other should be contained in the relevant disclosure document.⁹⁶

Section 602 of the Corporations Act sets out the underlying principles of fairness and disclosure of information in relation to the acquisition of shares, as well as emphasising the need for such acquisitions to occur in an efficient, competitive and informed market.⁹⁷

The Eggleston principles relate to:

- (a) sufficient time for shareholders to make a decision;
- (b) sufficient information to make a decision; and
- (c) reasonable and equal opportunities to share in any benefits that flow from a person acquiring a substantial interest in their company.⁹⁸

The Corporations Act requires that the bidder produce a Bidder's Statement and it be sent to all of the target company shareholders within set timeframes. The document must

⁹¹ Section 636(1)(m) of the Corporations Act. Damian and Rich, above n 2, 247.

⁹² Further, the takeover regulations are based on the Eggleston Committee's four principles, which are designed to ensure that the proposed takeover is in the best interest of the target shareholders as the owners of the company. The four Eggleston principles benefit the target shareholders as they ensure the following is provided: the identity of the party seeking control; a reasonable amount of information on which to base their offer; a reasonable amount of time to consider the offer; and, as far as possible, an equal opportunity for all shareholders to benefit from the bid.; Also see Damian and Rich, above n 11, 31-32.

⁹³ See section 636 of the Corporations Act for details.

⁹⁴ See ASIC RG 170.9 and 170.11.

⁹⁵ See for discussion between the intersection between the tests: the material information test and the reasonably informed investor test. Also see Re Primac Holdings Ltd.

⁹⁶ See judgment of Barrett J, RE HIH Casualty and General Insurance Limited (2006) 57ACSR 791 at 812 [81].

⁹⁷ Damian and Rich, above n 11, 31. They describe the tension between the operation of the Masel principle in section 602(a) of an 'efficient, competitive and informed market' and the operation of the Eggleston principles contained in the remainder of section 602 of the Corporations Act.

⁹⁸ Damian and Rich, above n 11, 31.

include a range of specific information in addition to the general disclosure of all information (including confidential information) known to the bidder that would be material to a decision regarding the acceptance of the offer.

The key specific disclosure requirements in a bidder's statement include: the identity of the bidder, including controllers and associates; the bidder's intention concerning the ongoing continuation of the target business,⁹⁹ the future employment of current employees, and details of the changes that may be made to the target business such as proposed restructurings or sale of non-core assets and if the bid price includes cash, details of the bidder's source of cash financing for the transaction.

In addition, if the bid price includes the issue of securities of the bidder or parent of the bidder, then the Bidder's Statement must also contain all the information that would be required in a prospectus for a public offer of those securities.¹⁰⁰

More specifically section 636 (1)(g) provides:

... if any securities ... are offered as consideration under the bid and the bidder is:

- (i) the body that has issued or will issue the securities; or*
- (ii) a person who controls that body;*

all material that would be required for a prospectus for an offer of those securities by the bidder under section 710 to 713;

Therefore a bidder in a takeover is required to provide as much information to the target members if they are issuing shares as any part of the consideration for the takeover as would a prospective investor would receive under a prospectus offer. Therefore it is necessary to examine the general and specific disclosure requirements for a prospectus offer under the Corporations Act.

⁹⁹ See *ICAL Ltd v. County Natwest Securities Ltd and Transfield (Shipbuilding) Pty Ltd* (1988) 6 A.C.L.C. 467 and *Cumberland Credit Corporation Ltd v. TNT Australia Pty Ltd* (1988) 6 A.C.L.C. 442. Prior to these decisions takeover documents contain very little information regarding future intentions, the Court found insufficient future intention information had been disclosed and required the offeror 'that if the offeror has considered alternative options but has determined not to make a final decision until such time as it has ascertained whether its takeover offer has been successful, then it is required to reveal these options to the shareholders'.

¹⁰⁰ See section 636(1)(g) of the Corporations Act.

Disclosure Obligations - Prospectus Offer

The Corporations Act contains detailed and intricate obligations for the disclosure of information for company fundraising activities through offers for sale or issue of securities to the general public.¹⁰¹ These general and specific disclosure requirements for a prospectus ensure retail investors and their professional advisors are capable of making an informed assessment of the proposed transaction. These disclosure requirements for fundraising activities are detailed in section 710 to section 713 of the Corporations Act.¹⁰² These disclosure requirements are intricate and impose both general¹⁰³ and specific disclosure¹⁰⁴ obligations for prospectus issuers to retail investors so that they are capable of making an informed assessment of the financial product. Section 636(1)(g) extends these prospectus disclosure obligations to bidder's statements that offer securities as either part of or all of the consideration in the bid price .

Prospectus disclosure requirements mandate that all material information be made available for prospective investors and their professional advisers would reasonably require to make an informed assessment.¹⁰⁵ This information covers the company's assets and liabilities; financial position and performance; profits and losses; the prospects of the company; and the rights and liabilities attaching to the company shares and the nature of the security interest being offered.¹⁰⁶

The "prospects of the company" refers to prospective information or forward-looking in nature¹⁰⁷ pertaining to the strategic and future plans of the bidder and that of the target moving forward. This prospective information can include financial information, non-financial information; details of future plans, strategy and opportunities that are available.

¹⁰¹ Chapter 6D of the Corporations Act and specifically sections 710 to 713.

¹⁰² section 710 (1) of the Corporation Act provides that: A prospectus for a body's securities must contain all the information that investors and their professional advisers would reasonably require to make an informed assessment of the matters set out in the table below. The prospectus must contain this information: (a) only to the extent to which it is reasonable for investors and their professional advisers to expect to find the information in the prospectus; and (b) only if a person whose knowledge is relevant (see subsection (3)): (i) actually knows the information; or (ii) in the circumstances ought reasonably to have obtained the information by making enquiries.

¹⁰³ Section 710(1) of the Corporations Act. There are some additional requirements in section 711 which relate mostly to the interests of those involved with the issuer and the preparation of the prospectus.

¹⁰⁴ Section 710 of the Corporations Act.

¹⁰⁵ Above n 21, 210.

¹⁰⁶ Above n 21, 213.

¹⁰⁷ See ASIC RG 170.2

Mandatory Disclosure of Prospective Information - Regime

It is a common perception of market participants that prospective information amounts to soft information disclosure, in particular, managerial profit forecasts. There is no mandatory¹⁰⁸ requirement for the disclosure of prospective information in takeover documents.¹⁰⁹ The issuer decision is based on balancing the information value (relevance) of what is disclosed against the likelihood that the information may be misleading (reliability).

Currently ASIC merely provides guidance as to whether prospective financial information can or should be disclosed.¹¹⁰ An issuer decides whether prospective financial information needs to be disclosed in a disclosure document¹¹¹ and in some sectors¹¹² prospective information is not provided at all. In other words the participants involved in a takeover have the final discretion in determining whether there are 'reasonable grounds' for the inclusion of the information.¹¹³

The increase in actions by ASIC and class actions relating to prospective information reinforces ASIC view that disclosure in the area needs to improved. In December 2010 ASIC released a report on the disclosure of financial information within financial reports of large listed entities in relation to profit disclosures. ASIC highlighted in its report that many of the entities failed to provide a reconciliation between the alternative and statutory profit figures;¹¹⁴ alternative¹¹⁵ profit was given more prominence than the statutory profit and many adopted alternative profit formats that was difficult to compare.

ASIC continues to release guidance papers on how better disclosure can be achieved by issuers for retail investors. In 2000, ASIC released Better Disclosure for Investors: Guidance Rules that incorporate 10 broad principles for companies to consider in the development of

¹⁰⁸ ASX Listed entities are subject to a range of mandatory disclosure obligations under Corporations Act.

¹⁰⁹ The Corporations Act enforces the accounting standards for the purpose of Ch 2M financial reports that are developed by the Australian Accounting Standards Board (AASB). There is no definition under the Corporations Act of prospective information.

¹¹⁰ See ASIC RG 170.2 and 170.3.

¹¹¹ See ASIC RG 170.7

¹¹² Many mining and IT companies that list on the ASX do not provide forecast information.

¹¹³ see ASIC RG 170.16.

¹¹⁴ For example, profit before tax (PBT), earnings before interest and tax (EBIT), earnings before interest, tax and amortisation (EBITA), and earnings before interest, tax, depreciation and amortisation (EBITDTA).

¹¹⁵ ASIC 2010 Review, n 6. More specifically, ASIC defines the term alternative profit disclosures to mean profits disclosed in a format not in accordance with International Financial Reporting Standards.

their disclosure policies.¹¹⁶ It is hard to imagine a situation that a forecast would never provide be of real and material assistance to investors. However, the party should not have the discretion to exclude prospective information¹¹⁷ but should be obligated to disclose the information and any related limitations to it. Management forecasts have been found to be more accurate than most forecasting models.¹¹⁸

Empirical research¹¹⁹ continues to show ASX listed companies¹²⁰ continue to provide inadequate disclosure of information in accordance with the periodic and continuous disclosure rules. This in part is due to the lack of a safe harbour for the release of forward looking statements.

During 2010 and 2011 ASIC released a series of guidance papers relating to company disclosure, including factors that should be considered to ensure that information released in the public arena is not misleading or deceptive.

ASIC in December 2011 released a Regulatory Guide 230 (RG 230)¹²¹ on disclosing financial information other than in accordance with accounting standards. It states that financial information that is presented other than in accordance with relevant accounting standards is being used increasingly in financial reports and other documents, such as transaction documents and market announcements. ASIC notes the risk that information that has not been prepared in accordance with IFRS¹²² will be misleading unless it is appropriately

¹¹⁶ ASIC, Better Disclosure for Investors: Guidance Rules (2000).

¹¹⁷ In off market takeovers preparing takeover documents is difficult in instances whether targets are privately held or limited information to known by the bidder or target.

¹¹⁸ C Westwick (ed), Profit Forecasts (Hants: Gower Publishing Company Ltd, 1983), p 155.

¹¹⁹ Bloch M, Weatherhead J and Webster J, "The Development and Enforcement of Australia's Continuous Disclosure Regime" (2011) 29 *Company and Securities Law Journal* 253. A review of the periodic disclosure regulation is provided in North G, "Periodic Disclosure Regulation: Enhancements to Enable All Investors to Make Informed Decisions?" (2009) 27 *Company and Securities Law Journal* 23

¹²⁰ The ASX listing rules in regards to forecasts only apply if a company has provided an actual forecast. Australian Securities Exchange (ASX), Guidance Note 8, Continuous Disclosure Listing Rule 3.1 (June 2005) 19. ASX Guidance Note 8 states: Listing Rule 3.1 provides examples of information that, if material, would require disclosure. One of those examples is a change in the entity's previously released financial forecast or expectations. As a general policy, a variation in excess of 10% to 15% may be considered material, and should be announced by the entity as soon as the entity becomes aware of the variation. If the entity has not made a forecast, a similar variation from the previous corresponding

¹²¹ While ASIC Regulatory Guides and Practice Notes do not have the force of law, they are indicative of the ASIC's views of the Law and of the way in which it will enforce the Law.

¹²² Australian Securities and Investments Commission Act 2001 (Cth), section 225.

presented and explained. Australian reporting entities have been required to report under IFRS since January 2005.¹²³

ASIC also release Regulatory Guide 228 (RG 228) in 2011 titled “Prospectuses: Effective disclosure for retail investors” that focuses on the content and form of prospectuses prepared under section 710 of the Corporations Act. ASIC has also nominated certain sections in the Regulatory Guide which it considers may apply to other documents commonly distributed to shareholders.¹²⁴

As a cornerstone Eggleston principle, sufficient information on the future prospects of the parties to a takeover must be mandated and not discretionary. Reform should introduce an agreed format of financial ratios, definitions, risks, assumptions and set time frames or periods.¹²⁵ Both forecasts and projections should be provided along with an analysis and comparison of these forms of prospective information. A forecast or projections should disclose the assumptions and future events built into the financial model to determine the prospective information, the extent of inquiries and research undertaken, the specific period to which it relates and an explanation for the choice of the period covered.

In Australia, earnings before interest and tax (EBIT) is generally the basis used for valuation purposes. However, globally the share markets trade based on profits after income tax. In the recent Vocation Limited initial public offering on the ASX their prospectus disclosed a historical net profit after tax (NPAT) was approximately \$4 million and contained a proforma¹²⁶ financial forecast profit after tax¹²⁷ increase to \$20m.¹²⁸ If financial forecasts can objectively show a 500% increase in net profit after tax within a 12 month time

¹²³ The Australian Accounting Standards Board (AASB) makes the accounting standards for the purpose of Chapter 2M financial reports and in doing so it may use or modify the text of international financial reporting standards (IFRS) issued by the International Accounting Standards Board (IASB).

¹²⁴ These documents include, transaction-specific prospectuses (eg Debentures); bidder’s statements under takeover offers; explanatory statements for schemes of arrangement; offer documents for “low doc” rights issues; and independent expert’s reports.

¹²⁵ In *Pancontinental* the court held that investors were entitled to the benefit of an earnings forecast for, at least, a two year period.

¹²⁶ See ASIC CP150 : Disclosing financial information other than in accordance with accounting standards para RG000.77. This may occur if that pro forma information includes information based on a hypothetical scenario.

¹²⁷ See ASIC CP150 : Disclosing financial information other than in accordance with accounting standards para RG000.77. This may occur if that pro forma information includes information based on a hypothetical scenario.

¹²⁸ See Vocation Limited Prospectus page 54 (viewed 15 December 2013 www.asx.com.au)

frame,¹²⁹ then this says something about the current requirements regarding the disclosure of prospective information in disclosure documents.

This 500% increase in NPAT could at best only be a projection based on hypothetical scenarios but it passes off as a forecast. However, it has satisfied ASIC prospective information disclosure requirements under RG 170 as a financial forecast. In this author's opinion, there must be a highly subjective judgement call on the future performance of the organisation. This prospectus content detailed on page 54 of the prospectus supports the view that ASIC should encourage more disclosure of prospective information in disclosure documents so as to allow investors to see a broader range of potential outcomes.

Takeover Liability and Defences

Liability concerns by bidders in delivering prospective information to target members reflects the boiler plate approach to industry practice which leads to a desensitised document that is less informative than may be potentially available. It is accepted that prospective information relies on a subjective opinion¹³⁰ on future events based on the expected outcomes of various assumptions.

The introduction of a mandatory disclosure regime for prospective information regime would be linked to a new stand-alone (safe-harbour) defence being made available to takeover participants that act appropriately. This would be a distinct and separate to any due diligence defence and statutory business judgment rule defence or relief potentially available under section 1318 of the Corporations Act.

In March 2000, Chapter 6B of the Corporations Act commenced operation to establish a stand-alone liability and defence regime for takeovers.¹³¹ Previously defective disclosure for takeovers was subject to the general misleading and deceptive provisions.¹³²

¹²⁹ This author is anxiously waits to see the half year results and full year results for Vocation Limited and any subsequent action by ASIC if the company fails to meet forecast profits.

¹³⁰ This needs to be clearly distinguished from presently existing statements of fact. As these facts have occurred and objectively ascertainable their truth or accuracy cannot be questioned.

¹³¹ Similarly section 731 of the Corporations Act provides due diligence defence to issuers and participants involved in the preparation of a prospectus offer. This defence applies if they made all reasonable inquiries and held a reasonable belief that the statements were not misleading and deceptive and contained no omissions. Under section 732 of the Corporations Act the onus is on the directors to prove on the balance of

Under section 670A(1), a person must not give:

- a takeover document if there is a misleading or deceptive statement in the document;
- a bidder's statement or target's statement if the document omits material required by the Corporations Act 2001 (Cth); or
- a bidder's statement or target's statement if a new circumstance that has arisen since the document was lodged would have been required by the Corporations Act (Cth) to be included in the document if it had arisen before the document was lodged.

A bidder can be subject to civil and criminal liability¹³³ for any misstatements in, and any omissions of relevant information from, a Bidder's Statement. This liability also extends to the company's directors¹³⁴ who approved the Bidder's Statement. Criminal liability can apply where a misstatement or omission was 'materially adverse' to the target shareholders. From the targets company and its directors perspective they can also be subject to civil and criminal sanctions in relation to misstatements or omissions in the target statement.

The Corporations Act provides similar due diligence defences to the company and its directors involved in a breach of takeover disclosure provisions. The due diligence defence will apply to a misstatement if the person who is facing liability had no knowledge that the statement was misleading or deceptive.¹³⁵ In the case of the omission of relevant information the due diligence defence will apply if the person did not actually know that there was an omission of relevant information.

The due diligence defences under section 670D provides that a person is not taken to have committed an offence under section 670A(3) if the person proves that they: did not know that a statement was misleading or deceptive; did not know there was an omission; placed reasonable reliance on information provided to them by a third party; removed their

probabilities that they did not know the statement in questions was misleading or deceptive, or they did not know the statement in question was misleading or deceptive.

¹³² Above n 11, 275.

¹³³ Sections 1041F(1) inducing another, 412(1) 670A and 670B of the Corporations Act.

¹³⁴ Section 670B of the Corporations Act 2001 imposes direct liability on directors for misstatements and omissions from takeover documents. Under section 79 of the Corporations Act proving accessory liability for contraventions need to satisfy a requirement of the person 'knowingly concerned in' the breach. The imposition of this mental intent element for accessorial liability is a difficult burden.

¹³⁵ Section 670A of the Corporations Act contains the misleading and deceptive provisions in relation to takeover documents.

consent to being named in the takeover document which contained the misleading or deceptive statement that was specifically attributable to them; or were unaware of a new circumstance that has arisen since the takeover document was lodged.¹³⁶

Prospective Information Defence

In addition to due diligence defence being available for takeover participants, since early 2000 Australia has had a statutory business judgment rule¹³⁷ as a defence to the care and diligence duty. It was designed to protect directors and officers who had acted in good faith with due care for contraventions to act with appropriate care and diligence.¹³⁸ Only recently has judicial attention been drawn to the defence in *ASIC v. Rich*.¹³⁹ The complicated four stage approach undertaken¹⁴⁰ highlights the concerns with this defence.¹⁴¹ Business groups consider that a business judgment defence is not appropriate in the context of personal liability for corporate fault.¹⁴²

In the United States, they have introduced the Private Securities Litigation Reform Act 1995 (the Reform Act) that supports for the introduction of a defence for prospective information in Australia. The US legislation provides a safe harbour for both written and oral forward-looking statements made by issuers, and their officers, directors, and employees; as well as underwriters and outside reviewers of the issuer, as well as a separate safe harbour that applies solely to oral forward-looking statements made by issuers, and their officers, directors, and employees.¹⁴³

¹³⁶ Tony Damian and Andrew Rich, *Schemes, Takeovers and Himalayan Peaks* (The University of Sydney, 3rd edition, 2013) 273 -274.

¹³⁷ Section 180(2) of the Corporations Act 2001.

¹³⁸ Andrew Lumsden, 'The business judgment defence: Insights from *ASIC v Rich*' (2010) 28 *Company and Securities Law Journal* 161.

¹³⁹ In *ASIC v Rich* [2009] NSWSC 1229 Austin J referred to the business judgment defence in s 180(2) as available 'to the management decisions involved in propounding a scheme of arrangement for the purposes of acquisition, or for purposes of corporate reconstruction'.

¹⁴⁰ See *Australian Securities and Investments Commission v Rich* [2009] NSWSC 1229 decision.

¹⁴¹ See Andrew Lumsden, 'The business judgment defence: Insights from *ASIC v Rich*' (2010) 28 *Company and Securities Law Journal* 161, 164; .

¹⁴² The Corporations and Markets Advisory Committee, 'Personal Liability for Corporate Fault', Report (September 2006) 59.

¹⁴³ Stephen Walker and Richard Kriedemann, 'Forecasts: Misleading or Essential?' (1997) 15 *Company and Securities Law Journal* 47, at 50 - 51.

The provision of projections of revenue, income, dividends and other financial information are included in the definition of forward-looking statements, together with any statements of the assumptions underlying forward-looking statements. Persons covered by safe harbour are not liable in connection with a forward-looking statement that is identified as forward-looking; and accompanied by meaningful cautionary statements which identify important factors which could cause actual results to differ materially from those projected in the statement.¹⁴⁴

In the light of the position in the USA, Australian Courts and ASIC actions, the author submit that a stand-alone defence be made available for takeover participants in regards to prospective information disclosed in takeover documents provided that have acted honestly and in good faith.

Prospective information is inherently, by virtue of their forward-looking character, considered to be an unreliable information type but is also highly relevant and useful.¹⁴⁵

Takeover participants should be encouraged to provide prospective information in takeover documents for investors and their professional advisors to have disparate views of the potential outcomes of the transaction proposed. The proposed reform of a safe harbour defence would greatly assist in this encouragement of this disclosure.

Takeover participants should provide information to enable the shareholders in the target company to form a judgment on the merits of the proposal.¹⁴⁶ Takeovers can result in a major disruption to the operations of the bidder and target business due to time, focus, number of participants¹⁴⁷ all of which occurs in a time sensitive¹⁴⁸ environment. This complexity is further enhanced¹⁴⁹ as issues arise concerning, confidentiality, valuation, ASX and ASIC compliance obligations and other issues that can distract management.¹⁵⁰

¹⁴⁴ Stephen Walker and Richard Kriedemann, 'Forecasts: misleading or essential?' (1997) 15 *Company and Securities Law Journal* 47, at 50 - 51.

¹⁴⁵ Above n 8, 350.

¹⁴⁶ Report of the Company Law Advisory Committee chaired by Sir Richard Eggleston (1969) Second Interim Report, paragraph 16.

¹⁴⁷ Including various individuals from the bidder, target, advisors experts, the court and regulators

¹⁴⁸ Section 633 of the Corporations Act details the steps in an off-market bid

¹⁴⁹ Takeovers involve tight deadlines to the distribution of information within strict timelines. See generally ASIC Regulatory Guides and ASX Listing Rules.

¹⁵⁰ Tatiana Stack 'Contractual basics in M&A for private business acquisitions in Australia' (2011) 8 *Macquarie Journal Business Law* 358, 366.

The Corporations Act should also be amended to include a new stand-alone defence for the disclosure of prospective information contained in takeover documents that is available to participants including bidders and targets, directors, officers and financial advisors. The Corporations Act currently provides several due diligence defences in respect of defective disclosure to takeovers and prospectus offers but not specifically for prospective information, i.e. forward looking statements. At present, liability arises in respect of takeover document if there is a misleading and deceptive statement or omits material information required or new circumstances are not disclosed.

A mandatory disclosure regime for prospective information in takeover documents was to be imposed so that both financial forecasts and financial projections were provided, then retail investors would have access a wider variety of potential judgments that detailed a broader range of potential outcomes from the transactions.

A number of business groups including the Australian Institute of Company Directors (AICD), the Business Council of Australia (the BCA) and the Law Council of Australia (the LCA), have campaigned for the establishment of a safe harbour¹⁵¹ that can be readily utilised by directors and senior officers.¹⁵²

The increasing range of provisions under the Corporations Act that impose penalties and sanctions upon directors, officers and advisers¹⁵³ for conduct undertaken during their service to the company that may be dampening entrepreneurial spirit.¹⁵⁴

Section 1318 of the Corporations Act

The need for a safe harbour for prospective financial information in takeovers is further supported by the interpretation and application of relief from liability under section 1318 of the Corporations Act.

¹⁵¹ The AICD, the BCA, the LCA have campaign to persuade the Federal Government to introduce a softer and more relevant statutory business judgment rule.

¹⁵² Editorial (2013) 31 *Company and Securities Law Journal* 471.

¹⁵³ Breen Haire, 'The Fiduciary Responsibilities of Investment Bankers in Change-of-Control Transactions: In Re Daisy Systems Corp' (1999) 74 *New York University Law Review* 277 at 287-288.

¹⁵⁴ Young, Neil, 'Has Directors' Liability Gone Too Far or Not Far Enough? A Review of the Standard of Conduct Required of Directors Under Sections 180-184 of the Corporations Act' (2008) 26 *Company and Securities Law Journal* 216; Jason Harris and Suzanne Webbey, 'Personal liability for corporate disclosure problems' (2011) 29 *Company and Securities Law Journal* 463.

Recent decisions that imposed liability on directors that acted honestly further supports the introduction of a defence regime for prospective information disclosed in takeover documents. Leading commentators¹⁵⁵ are astonished at the hard line judges have taken in granting relief under section 1318 for conduct undertaken honestly and in good faith.¹⁵⁶ The Court has power to grant relief from liability for contravention of civil penalty provision¹⁵⁷ and the power to grant relief from liability for contravention of civil penalty in respect of negligence, default, breach of trust or breach of duty.¹⁵⁸

In the *Centro*, Middleton J, found that even though the financial accounts had been audited by PWC,¹⁵⁹ the directors had failed in their duties to exercise the degree of care and diligence required of them.¹⁶⁰ The directors are entitled to rely on management and auditors but such reliance cannot be a substitute for their own non-delegable responsibilities.¹⁶¹ Middleton J, found that there was no suggestion that each director did not act honestly or that the contraventions involved knowledge on the part of any director that he was acting wrongly. In his penalties decision,¹⁶² Middleton J considered whether this was a mitigating factor for the directors. Owing to the seriousness of the contraventions, Middleton J, was not prepared to grant the directors' applications for relief from liability under ss 1317S or 1318. The Court has the discretion to relieve the person from liability if it appears that the person has acted honestly having regard to all the circumstances.

His Honour stated that a person acts honestly if the person's conduct is without moral turpitude that is without deceit or conscious impropriety; without intent to gain an

¹⁵⁵ Robert Baxt, 'Policy Somersaults on Directors' Duties – Disappointment and Dismay in the Business Community' (2011) 7 *The Baxt Report* 6; Robert Baxt, 'The James Hardie decision – the penalty decision: honesty is apparently the best policy!' (2009) 5 *The Baxt Report* 1.

¹⁵⁶ Carr v Resource Equities Ltd [2010] NSWCA 286

¹⁵⁷ Under the Corporations Act s. 1317S.

¹⁵⁸ Under the Corporations Act s. 1318. This section applies to a person who is: (a) an officer or employee of a corporation; or (b) an auditor of a corporation, whether or not the person is an officer or employee of the corporation; or (c) an expert in relation to a matter.

¹⁵⁹ PWC was successfully sued by class action lawyers Maurice Blackburn and Slater + Gordon.

¹⁶⁰ Andrew McRobert and Ronnie Hoffman, *Financial Literacy: Lessons from Centro* (Thomson, 2011) 3-7.

¹⁶¹ Justice Middleton cited the judgment of Santow J in *Australian Securities and Investments Commission v Adler* [2002] 168 FLR 253 at 372.

¹⁶² *Australian Securities and Investments Commission v Healey (No 2)* (2011) 196 FCR 430 at [132]-[142].

improper benefit or advantage; and without carelessness or imprudence that negates the performance of the duty in question.¹⁶³

If the person is found to have acted honestly then the matters to be considered to determine if the discretion out to exercise "... include the degree to which the person's conduct fell short of the statutory standard of care and diligence, the seriousness of the contravention and its potential or actual consequences, impropriety such as deceptiveness or personal gain and contrition.¹⁶⁴

It appears that the Courts are currently reluctant¹⁶⁵ to exercise their discretion in granting relief to persons that have acted honestly and in good faith.¹⁶⁶ In many instances various takeover participants¹⁶⁷ such as directors and management are swept along due to time constraints placing heavy reliance on investment bankers, takeover lawyers, independent experts, investigating accountants and auditors.

Conclusion

In light of the above, the author submits that the time has come for takeover documents laws to be amended to impose a mandatory disclosure regime for prospective information including forecasts and projections in takeover documents. The provision of sensitivity analysis¹⁶⁸ performed on prospective information would detail the range of potential outcomes of the transaction and could allow better decisions to be made by shareholders and investors.¹⁶⁹ Retail investors are assisted by the disclosure of prospective information that has been subject to sensitivity analysis as this provides access to a range of potential outcomes so that they can arrive at a more informed independent decision.

¹⁶³ Australian Securities and Investments Commission v Healey (No 2) (2011) 196 FCR 430 at [88].

¹⁶⁴ Australian Securities and Investments Commission v Healey (No 2) (2011) 196 FCR 430 at [89]. As to penalties generally his honor provides deterrence is both specific "...where the punishment is sufficiently unpleasant to deter the person from committing further breaches of the law, and general deterrence where the punishment is set to deter potential offenders from committing that offence."

¹⁶⁵ Editorial, 'Significant Developments' (2012) 40 *Australian Business Law Review* 137, 139.

¹⁶⁶ Robert Baxt, 'The James Hardie Saga – The Final Curtain' (2013) 9 *The Baxt Report* 1.

¹⁶⁷ The onus is always on the director to establish either that the statutory business judgment should be applied or alternatively that discretion to award relief should be exercised by a judge.

¹⁶⁸ Is a financial analysis approach against expected outcomes and allows what if scenarios to be undertaken and its resulting outcome. See Simon Benningna, 'Financial Modelling', The MIT Press, 2nd edition, 2010, 71.

¹⁶⁹ Section 633 of the Corporations Act details the steps in an off-market bid

This regime shall provide a safe-harbour defence for takeover participants that have acted honestly and in good faith in relation to prospective information disclosed. A defence for disclosure of prospective information in takeover documents would enhance the quality as well as usefulness and reliability of information to retail investors and shareholders, while ensuring financial innovation and entrepreneurial spirit continues to flourish in Australia, by addressing liability concerns.

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