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Federal Court Delivers Decision on “Naked No Vote” Break Fees

On 10 December 2007, the Federal Court in *Bolnisi Gold NL (No 2)* [2007] FCA 2078 delivered a judgment which provides guidance on “naked no vote” break fee provisions in the context of takeovers and schemes of arrangement. A “naked no vote” break fee is a break fee which is payable by a target to a bidder where the takeover or scheme is rejected by the target’s shareholders, despite the absence of any competing offer from another bidder.

The case concerned a proposed scheme of arrangement under which Coeur d’Alene Mines Corporation (“**Coeur**”) offered to acquire all of the shares in Bolnisi Gold NL (“**Bolnisi**”). In his judgment, Justice Lindgren commented that it would be appropriate for the court to decline to order that a scheme meeting be convened, or that a scheme be approved, if the court is satisfied that a “naked no vote” break fee is so large as to be likely to coerce shareholders into agreeing to the scheme – in order to avoid the target becoming liable to pay the “naked no vote” break fee – rather than allowing shareholders to assess the offer on its merits.

The court took into account the approach in the United States regarding break fees – which is similar to the approach taken in Australia. In the US decision of *Williams v Geier* 671 A.2d 1368 (Del Supr 1996) it was considered that wrongful coercion that nullifies a stockholder’s vote may exist “*where the board or some other party takes actions which have the effect of causing the stockholders to vote in favor of the proposed transaction for some reason other than the merits of that transaction*”.

The Takeovers Panel in Australia considered “naked no vote” break fees in *Ausdoc Group Ltd* (2002) 42 ACSR 629. In that decision, the Panel agreed with submissions from the Australian Securities & Investments Commission that “naked no vote” break fees should be distinguished from other forms of break fees which are payable where the bid does not succeed due to a higher rival bid. This is because in a “naked no vote” situation there is no rival bidder which could help fund the cost of the break fee payable to the unsuccessful bidder.

In *Bolnisi Gold NL* it was held that the “naked no vote” break fee provision was not objectionable for the purposes of Bolnisi’s application under section 411 of the Corporations Act 2001 (Cth). Section 411 deals with the court’s approval to convene a meeting of shareholders to vote on a proposed scheme of arrangement. The court took into account the following factors in arriving at this decision:

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- the amount of the break fee would not exceed the costs and expenses related to the proposed scheme incurred by Coeur;
- the directors of Bolnisi believed that they were acting in the best interests of the shareholders of Bolnisi in agreeing to the “naked no vote” break fee;
- the fact that there was also a break fee of the same amount payable by Coeur to Bolnisi in the event that the shareholders of Coeur did not resolve that shares in Coeur, being the scheme consideration, be issued to Bolnisi’s shareholders;
- it was important for Bolnisi to have the benefit of the above break fee payable by Coeur and, to obtain Coeur’s agreement to that break fee, Bolnisi was, in turn, required to agree to the “naked no vote” break fee;
- the amount of the “naked no vote” break fee was less than the 1% of the equity value of Bolnisi – consistent with the Takeovers Panel’s Guidance Note 7 on lock up devices – and could not be regarded as so large as to be likely to coerce shareholders into voting in favour of the scheme; and
- the respective break fees and the other lock up devices used in the transaction were agreed to by the parties following arm’s length commercial negotiations over a period of one month in which each of Bolnisi and Coeur consulted separate advisers with relevant expertise in the area.

Whilst “naked no vote” break fee provisions are not prima facie invalid, the decision in *Bolnisi Gold NL* highlights that the court will carefully consider the facts of each case to ensure that such a break fee is not contrary to the interests of the target or its shareholders and, therefore, unenforceable. In essence, parties seeking to rely on the benefit of a “naked no vote” break fee must ensure that, in all the circumstances, the amount and other terms applicable to that fee are not such as to coerce the target shareholders to agree to the offer, irrespective of the underlying merits of that offer. The Takeovers Panel is also likely to take guidance from this decision in determining applications involving “naked no vote” break fees.

For more information please contact:

David P. Selig, Partner

Telephone: +61 2 8915 1010

Facsimile: + 61 2 8916 2010

Email: david.selig@addisonslawyers.com.au

Nathan Greenfield, Solicitor

Telephone: +61 2 8915 1042

Facsimile: + 61 2 8916 2042

Email: nathan.greenfield@addisonslawyers.com.au