Strong Australian Dollar Shines Spotlight
On New Foreign Currency Rule

In brief

- The strong Australian dollar has brought foreign currency takeover bids into sharp focus, with the Takeovers Panel resolving a debate that has been running since CEMEX's US dollar bid for Rinker in 2006.
- The Panel has confirmed that foreign bidders bear exchange rate risk if they acquire a pre-bid stake in the target.

The Panel has recently resolved the long-running debate on the application of the minimum bid price rule to foreign currency bids. This development in takeover policy has significant implications for foreign currency takeover bids.

If a bidder makes an offer under a takeover bid it must pay at least the amount it paid for a pre-bid purchase made within four months prior to the bid. Bid consideration can be in the form of cash, scrip or a mix of the two.

Cash bids, because of their set value, only require a simple comparison between the pre-bid acquisition price and the bid offer price for the purposes of the minimum bid price rule. Scrip bids, on the other hand, must be valued at the time the bidder's statement is sent to shareholders and then compared to the pre-bid purchase value.

The Panel has confirmed that foreign currency will be treated like scrip for takeover purposes. If a bidder acquires a pre-bid stake and then follows up with foreign currency as bid consideration, it will need to compare the value of its pre-bid stake acquired in Australian dollars, against the Australian dollar equivalent value of the bid at the beginning of its offer period. This means that the bidder will bear the exchange rate risk in the interim.

Rinker revived

In 2006, Mexican company CEMEX made a A$16.8 billion hostile takeover bid for the buildings material company Rinker Group.* The initial price offered was US$13 per share. CEMEX purchased 1000 Rinker shares at A$14 per share prior to this bid. One of the contentious issues in the bid was that the offer was made in US dollars, despite the pre-bid acquisition being made in Australian dollars. Shareholders' equivalent Australian dollar consideration declined during the offer period as a result of the appreciating dollar.

The Panel required CEMEX to make supplementary disclosure about the currency and execution risks associated with the use of foreign currency. These risks included that:

- there may be a significant shift in the exchange, which may affect the value of the offer in Australian dollars
- different shareholders who accept the offer on different days may receive different Australian dollar amounts
- the exchange rate prevailing on the day a particular shareholder accepted the offer may differ from the rate prevailing at the time of payment, and
- CEMEX's own trading strategy may contribute to exchange rate fluctuations and how they were planning to limit their effect.

The Panel left open the issue of how a foreign currency bid would be treated under the minimum bid price rule. This was partly because CEMEX had given undertakings to the Panel not to make any further on-market purchases in Australian dollars during the bid.

Foreign currency – cash v scrip

The minimum bid price rule treats cash and scrip bids differently. Cash bids do not need to be valued for the purpose of comparing the offer price to the pre-bid acquisition price. Scrip bids, on the other hand, need to be valued so that the implied offer price per share can be compared to the pre-bid acquisition price. According to ASIC policy, scrip is valued at the beginning of the offer period for this purpose, that is, when the bidder's statement is sent to shareholders.

The Panel has ruled that foreign currency bids will be treated like scrip bids for this purpose. A bidder who offers foreign currency as bid consideration must compare the Australian dollar value of their pre-bid acquisition to the Australian dollar value of the offer at the time the bidder's statement is sent. A bidder may have to top-up shareholders to reach the pre-bid amount paid and satisfy the minimum bid price rule.

For example: A bidder has made a pre-bid purchase at A$10 per share offers US$10 per share under a takeover bid when the Australian dollar is at parity. As a result of an appreciating dollar, the Australian dollar equivalent of the bid offer has decreased to A$9 per share. To satisfy the minimum bid price rule, the bidder will have to increase the price offered under the bid to ensure the equivalent Australian dollar amount is equal to A$10 per share.

As the example illustrates, the implied Australian dollar value of an offer will be the baseline for the application of the minimum bid rule. This places the burden of the exchange rate risk firmly on the shoulders of foreign bidders.

Future for foreign currency bids

Foreign bidders who acquire a pre-bid stake in the target and use foreign currency as bid consideration bear the burden of exchange rate fluctuations between acquiring a pre-bid stake and sending the bidder's statement to shareholders. If they do not acquire pre-bid stake, target shareholders can continue to bear the foreign exchange rate risk, as long as the bidder adequately discloses the associated risks.

* Freehills acted for Rinker in relation to the CEMEX takeover bid.

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