

Companies (Minority Buy-out Rights) Amendment Bill

Government Bill

As reported from the Commerce Committee

Commentary

Recommendation

The Commerce Committee has examined the Companies (Minority Buy-out Rights) Amendment Bill and recommends that it be passed with the amendments shown.

Introduction

This bill amends the Companies Act 1993 to clarify and improve the existing minority buy-out regime. The bill provides an exit regime for dissenting shareholders who oppose fundamental changes to the company's structure—a special resolution. Once a special resolution has been made and the dissenting shareholder has made a request for the company to purchase its shares, the bill provides guidance on determining an appropriate price for those shares.

The majority of submissions on the bill were supportive of its general intent of clarifying the minority buy-out regime.

This commentary focuses on the major issues we examined and the amendments recommended. We also recommend some amendments

to clarify the intent of the bill, and other minor changes, which are not discussed.

Share valuation methodology

We recommend retaining the requirement for a company to use a “fair and reasonable” valuation method for determining the price it is willing to pay for shares. We consider this test is well established and requires an objective assessment of value.

The minority buy-out provisions of the Companies Act 1993 require that a company adopt a “fair and reasonable” valuation method, which will result in a “fair and reasonable” price, when determining the price it is willing to pay for the shares. After Justice Doogue’s criticism in *Natural Gas Corporation Holdings Ltd v Infratil 1998 Ltd*¹ that the existing regime was lacking in information for shareholders, particularly as to the valuation method and date, a review was undertaken of the regime. This resulted in proposed new section 112(2) (clause 7), which specifies that the company must adopt an “honest estimate” approach when applying the valuation method.

We agree with those submitters who opposed this approach because it involves a subjective assessment of value, and provides no judicial guidance as to its meaning so the valuation method is not clear.

Date of valuation

We recommend amending proposed new section 112(2) (clause 7) to provide that the value of the shares being purchased by a company be determined at the close of business on the day before the day on which the resolution was passed. As introduced, proposed new section 112(2) provides for valuation on the date the board gives notice to the minority shareholder agreeing to purchase the shares. The problems with this valuation date are that it would require both the shareholder and the company to anticipate events, and that it could result in different shareholders having different valuation dates.

¹ *Natural Gas Corporation Holdings Ltd v Infratil 1998 Ltd* [2000] 3 NZLR 727, 728 (HC).

Exception to valuation methodology

Proposed new section 112(3) (clause 7) of the bill as introduced provides an exception to the default valuation method in new section 112(2) only when a special resolution relates to a potential amalgamation. We recommend broadening this exception to allow the use of a different method whenever the default valuation method would be “clearly unfair” to either the shareholder or the company.

Arbitration determinations in cases of objection

Proposed new section 112A (clause 7) of the bill as introduced allows a price to be determined through arbitration if the shareholder and the company cannot come to an agreement on the purchase price.

We recommend that proposed new section 112A(6) be amended to ensure that the provisions of the Arbitration Act 1996 are applied when a matter is referred to arbitration. We further recommend amending proposed new section 112A(1) to make it clear that either party could initiate arbitration, not just the company.

Some submitters were concerned that proposed new section 112A(4) allows the arbitrator to award a shareholder damages for any shortfall in the initial payment, whether or not the shortfall was foreseeable. We recommend deleting “whether foreseeable or not”, as it is not appropriate for a person to be held liable for effects they could not foresee.

Interest awards

We agree with submitters who argued that proposed new section 112B(1) (clause 7), in prescribing the Judicature Act 1908 interest limits for any outstanding balance, does not allow market fluctuations in interest rates to be accounted for. We recommend amending proposed new section 112B(1) to delete the reference to the Judicature Act 1908 and to allow the arbitrator the discretion to award an appropriate interest rate.

Passing of legal and beneficial title

We recommend amending proposed new section 112C(1) (clause 7) to provide that legal title to shares passes to a company on notification of the company’s decision to purchase the shares. The reference to

beneficial interest in the clause as introduced has been removed. This is consistent with common law, in that beneficial title in property passes at the time a contract for sale has been made. The arbitrator's ability to award damages should provide the company with sufficient incentive to avoid delays in offering an adequate price.

As introduced, proposed new section 112C(1) provides for legal and beneficial title of the shares to remain with the shareholder until the price is ascertained and paid in full, to give the company an incentive to offer an adequate price and to prevent delays if valuation were to go to arbitration.

Legal title to the shares gives shareholders three rights: to vote on company decisions, to make distributions of the shares, and to receive distributions of the shares. It is inconsistent for the shareholder to retain these rights once they have elected to be bought out of the company.

Our proposed amendment to new section 112C(1) means that the restrictions on disposition of legal title to, or beneficial ownership of, shares contained in new section 112C(2) are no longer needed, and we recommend that these be removed.

Appendix

Committee process

The Companies (Minority Buy-out Rights) Amendment Bill was referred to the committee on 11 December 2007. The closing date for submissions was 29 February 2008. We received and considered five submissions from interested groups and individuals. We heard four submissions.

We received advice from the Ministry of Economic Development.

Committee membership

Gerry Brownlee (Chairperson)

Gordon Copeland (Deputy Chairperson)

Dave Hereora

Hon Darren Hughes (until 2 April 2008)

Hon Luamanuvao Winnie Laban

Simon Power

Hon Mita Ririnui (from 2 April 2008)

Hon Paul Swain

Lindsay Tisch

Dr Richard Worth

**Companies (Minority Buy-out Rights)
Amendment Bill**

Key to symbols used in reprinted bill

As reported from a select committee

text inserted unanimously

~~text deleted unanimously~~

Hon Lianne Dalziel

Companies (Minority Buy-out Rights) Amendment Bill

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The Parliament of New Zealand enacts as follows:

1 Title
This Act is the Companies (Minority Buy-out Rights) Amendment Act **2007**.

2 Commencement 5
This Act comes into force on the day after the date on which it receives the Royal assent.

**Part 1
Amendments to Companies Act 1993**

3 Principal Act amended 10
This Part amends the Companies Act 1993.

4 Company may acquire its own shares
Section 58 is amended by omitting “to 112 of this Act” in each place where it appears and substituting in each case “to **112C**”.

5 Cancellation of shares repurchased 15
Section 66(1) is amended by omitting “section 112 of this Act” and substituting “**sections 112 to 112C**”.

6 Company may hold its own shares
Section 67A is amended by omitting “section 112 of this Act” in each place where it appears and substituting in each case “**sections 112 to 112C**”.

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7 New sections 112 to 112C substituted
Section 112 is repealed and the following sections are substituted:

“112 **Valuation of Price for shares to be purchased by company determined**

“(1) Within 5 working days of giving notice under section 111(2)(e) that the board agrees to the purchase of shares by the company, the board must give to the holder of ~~those~~ the shares written notice of—

“(a) the price it offers to pay for those shares; and

~~“(b) how the matters in **subsection (2)(a) and (b)** were calculated.~~

“(b) how—

“(i) the matters in **subsection (2)** were calculated;
or

“(ii) the price was calculated under **subsection (3)** and why calculating the price using the methodology set out in **paragraphs (a) to (c) of subsection (2)** would be clearly unfair.

“(2) That price must be ~~an honest estimate of the value (on the date that the board gave notice under section 111(2)(e)) of a fair and reasonable price (as at the close of business on the day before the date on which the resolution was passed) for~~ the shares held by the shareholder, calculated as follows:

“(a) first, the fair and reasonable value of the total shares in each class to which the shares belong must be calculated (the **class value**):

“(b) secondly, each class value must be adjusted to exclude any fluctuation (whether positive or negative) in the class value that has occurred (whether before or after the resolution was passed) that ~~the board reasonably considers~~ was due to, or in expectation of, the event proposed or authorised by the resolution (~~see **subsection (7)**~~):

“(c) thirdly, a portion of each adjusted class value must be allocated to the shareholder in proportion to the number of shares he, she, or it holds in the relevant class.

“(3) However, if the resolution approved an amalgamation of the company under section 221, ~~no adjustment of value may be made under **subsection (2)(b)** in respect of any shares (whether comprising part, or the whole, of a class of shares) that—~~

- “(a) will not be converted into shares of the amalgamated company; and
- “(b) the board reasonably considers increased in value due to, or in expectation of, the amalgamation proposed or authorised by the resolution. 5
- “(3) However, a different methodology from that set out in **paragraphs (a) to (c) of subsection (2)** may be used to calculate the fair and reasonable price for the shares if using the methodology set out in those paragraphs would be clearly unfair to the shareholder or the company. 10
- “(4) The shareholder may object to the price offered by the board for the shares by giving written notice to the company no later than 10 working days after the date on which the board gave written notice to the shareholder under **subsection (1)**.
- “(5) If the company does not receive an objection to the price in accordance with **subsection (4)**, the company must purchase all the shares at the nominated price no later than 10 working days after— 15
 - “(a) the date on which the board’s offer under **subsection (1)** is accepted; or 20
 - “(b) if the board has not received an acceptance, the date that is 10 working days after the date on which the board gave written notice to the shareholder under **subsection (1)**.
- “(6) The time periods in **subsection (5)** do not apply if there is a written agreement between the board and the shareholder that specifically sets a different date for purchase of the shares. 25
- “(7) In this section, **resolution** means the resolution referred to in section 110 or 118 that, due to it having been passed, entitles the shareholder to require the company to purchase the shareholder’s shares in accordance with section 111. 30

- “**112A Share valuation Price for shares referred to arbitration if shareholder objects to price**
- “(1) If a company receives an objection to the price offered for shares in accordance with **section 112(4)**, the company must— 35

- “(a) ~~refer~~ the following issues must be submitted to arbitration ~~for determination~~:
- “(i) ~~the value of~~ fair and reasonable price for the shares, on the basis set out in **section 112(2) and (3)**; and 5
- “(ii) the remedies available to the holder of the shares or the company in respect of any ~~share valuation price for the shares~~ that differs from that determined by the board under **section 112**; and
- “(b) the company must, within 5 working days of receiving 10 the objection, pay to the shareholder a provisional price in respect of each share equal to the price offered by the board under **section 112(1)**.
- “(2) If the price determined for the shares—
- “(a) exceeds the provisional price paid, the arbitral tribunal 15 must order the company to pay the balance owing to the shareholder:
- “(b) is less than the provisional price paid, the arbitral tribunal must order the shareholder to pay the excess to 20 the company.
- “(3) Except in exceptional circumstances, an arbitral tribunal must award interest on any balance owing or excess to be paid under **subsection (2)**.
- “(4) If a balance is owing to the shareholder, an arbitral tribunal may award to the shareholder, in addition to or instead of an 25 award of interest, damages for loss (~~whether foreseeable or not~~) attributable to the shortfall in the initial payment.
- “(5) Any sum that must be paid in accordance with this section must be paid no later than 10 days after the date of the arbitral tribunal’s determination, unless the arbitral tribunal specifically 30 orders otherwise.
- “(6) A ~~reference~~ submission to arbitration under this section is an arbitration agreement for the purposes of the Arbitration Act 1996, and the provisions of that Act apply accordingly.
- “(7) Clause 6 of Schedule 2 of the Arbitration Act 1996 may not be 35 excluded from the arbitration agreement, and the term ‘costs and expenses of an arbitration’ in that clause includes, where a balance is owing to the shareholder,—

- “(a) the reasonable legal costs of the shareholder on a solicitor-and-client basis; and
- “(b) the reasonable costs of expert witnesses.

“112B Interest payable on outstanding payments

- “(1) Interest is payable on any sum that must be paid under **section 112 or 112A** that is outstanding after the date on which it falls due—
- “(a) on a daily basis until the date of full payment; and
 - “(b) at the prescribed rate (within the meaning of section 87(3) of the Judicature Act 1908) on the date the outstanding payment is made.
- “(1) Interest is payable on any sum that must be paid under **section 112 or 112A** that is outstanding after the date on which it falls due on the basis and at the rate that the arbitral tribunal thinks fit having regard to all of the circumstances.
- “(2) The sum on which interest is payable under **subsection (1)** includes any interest or damages for loss awarded under **section 112A**.

“112C Restrictions on, and timing of, transfer of shares

- “(1) The legal title to, and the beneficial ownership of, shares purchased by a company in accordance with section 111(2)(a) pass to the company,—
- “(a) if the company does not receive an objection to the price offered for the shares in accordance with **section 112(4)**; when that price has been paid in full; or
 - “(b) if the company receives an objection to the price offered for the shares in accordance with **section 112(4)**,—
 - “(i) when the balance owing to the shareholder in accordance with **section 112A(2)(a)** has been paid in full; or
 - “(ii) if an arbitral tribunal agrees with the board’s valuation of the shares; on the date of the tribunal’s determination; or
 - “(iii) if an order is made under **section 112A(2)(b)**; upon the making of that order.
- “(2) After a shareholder has given notice under section 111(1) requiring a company to purchase the shareholder’s shares; pur-

ported dispositions of the legal title to, or the beneficial ownership of, those shares (other than dispositions in favour of the company) have no effect.

“112C Timing of transfer of shares

- “(1)** On the day on which a board gives notice under section 111(2)(e) that the board agrees to the purchase of shares by the company,— 5
- “(a)** the legal title to those shares passes to the company; and
- “(b)** the rights of the shareholder in relation to those shares end. 10
- “(2)** However, for the purposes of **sections 112 and 112A**, **shareholder** and **holder of the shares** means the person who held the legal title to the shares immediately before the board gave notice under section 111(2)(e) that the board agrees to the purchase of those shares by the company. 15
- “(3)** **Subsection (2)** applies despite **subsection (1)**.”

8 Purchase of shares by third party

Section 113(1) is amended by omitting “Section 112 of this Act applies” and substituting “**Sections 112 to 112C** apply”.

9 Schedule 1 amended 20

Clause 2(2) of Schedule 1 is amended by adding “; and” and also by adding the following paragraph:

- “(c)** in the case of special resolutions required by section 106(1)(a) or (b), the right of a shareholder under section 110.” 25

Part 2

Transitional provision and consequential amendments to other enactments

10 Application of amendments in Part 1 30

The amendments in **Part 1** do not apply to any special resolution passed under section 106(1) of the Companies Act 1993 before this Act comes into force.

11 Amendment to Co-operative Companies Act 1996

- (1) This section amends the Co-operative Companies Act 1996.
- (2) Section 29(f) is amended by omitting “112 and” and substituting “**112** to”.

12 Amendment to Overseas Investment Regulations 2005

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- (1) This section amends the Overseas Investment Regulations 2005.
- (2) Regulation 33(1)(b)(ii) is amended by omitting “section 112” and substituting “**sections 112 to 112C**”.

Legislative history

7 November 2007
11 December 2007

Introduction (Bill 167–1)
First reading and referral to Commerce Committee

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