

Article Information

Author: Lis Boyce

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Bidding Battle for Virtus - Takeovers Panel Weighs In

ASX listed provider of assisted reproductive services, Virtus Health Limited has been the subject of intense interest from two suitors:

- CapVest Partners LLP (CapVest); and
- BGH Capital as manager and adviser to entities of the BGH Capital Fund 1 (BGH).

since December last year.

The competing bids have been accompanied by various approaches to the Takeovers Panel.

This article focuses on the Takeovers Panel's reasons for a finding of unacceptable circumstances with respect to particular aspects of a "Process Deed" between Virtus and CapVest^[1].

Key events leading up to the Panel deliberations

From the ASX announcements and the Panel's published reasons, the key events were:

Date	Event
14 December 2021	Virtus announces an unsolicited non-binding indication of interest from BGH-: \$7.10 per share
17 December 2021	Meeting between BGH and Virtus
22 December 2021	Virtus tells BGH that Virtus would consider BGH's proposal and reconnect in January 2022
20 January 2022	Virtus announces it had received a non-binding indicative bid from CapVest - \$7.60 per share (if the transaction proceeded by Scheme of Arrangement) or \$7.50 (by an alternative such as an off market takeover) - and signed a Process Deed
2 February 2022	BGH applies to Panel for declaration of unacceptable circumstances concerning exclusivity arrangements in the Process Deed
23 February 2022	Panel makes declaration of unacceptable circumstances
24 February 2022	Virtus announces an amended Process Deed with Capvest
13 April 2022	Panel publishes reasons for decision of unacceptable circumstances

Reasons for decision

The Panel declared that circumstances in connection with the original Process Deed between CapVest and Virtus were unacceptable, concluding that the exclusivity arrangements overall would inhibit or be likely to inhibit the acquisition of control over voting shares in Virtus taking place in an efficient, competitive and informed market. The Panel ordered that Virtus and CapVest not enter into a scheme implementation agreement for a certain period of time and that certain exclusivity arrangements would be ineffective unless they were changed to clarify the "fiduciary out"^[2].

What were the exclusivity arrangements?

Under the Process Deed:

- CapVest was entitled to exclusivity for “forty business days after Data Room Open Date”.
- Virtus was obliged to notify CapVest of any Competing Proposals, including all material terms and the identity of the proposing entity so that CapVest would have an opportunity to provide a matching or superior proposal. Virtus had to allow CapVest 5 business days to provide the matching or superior offer. Virtus had to give reasonable consideration to the CapVest counter-proposals and notify CapVest of their response within 2 business days and, if the Virtus board decided that the CapVest counter-proposal was acceptable, the parties had 3 business days to use best endeavours to settle the transaction documentation for the CapVest counter-proposal.
- the “fiduciary out” only came into force 15 Business Days after the Data Room Open Date.
- Virtus promised to provide CapVest with any known undisclosed information about Virtus’ business which it provided to any other party in connection with an alternative proposal and which had not already been provided to CapVest.

What were the key concerns?

The likely timing of the Data Room Open Date was not disclosed by Virtus in its announcement on 20 January 2022. The Panel found that Guidance Note 7[3] — *“the existence and nature of any lock-up device should normally be disclosed when the relevant control proposal is announced”* was not followed because the Exclusivity Period was tied to the Data Room Open Date which was not disclosed in the Virtus announcement.

Guidance note 7 states that *“in the absence of a effective ‘fiduciary’ out, a no-talk restriction is likely to give rise to unacceptable circumstances”*. The process deed effectively precluded the board of Virtus from exercising the “fiduciary out” during the period 20 January 2022 to 20 February 2022. The Panel found that the lack of the “fiduciary out” for part of the exclusivity period would likely reduce the potential for an alternative proposal.

The Panel also considered that it was unclear whether the “fiduciary out” truly existed in circumstances where:

- CapVest could match a genuine competing proposal with another non-binding proposal; and
- CapVest’s ability to match or exceed any genuine competing proposal each time one was made could mean that the competing proposal never became a Superior Proposal and therefore could not trigger a “fiduciary out” at all.

With respect to Virtus’ obligation to share any information that it had not already shared with CapVest when it shared it with another bidder, the Panel accepted that the directors of the target have the right and obligation to use it in the best interest of the company. However, the Panel found that this provision could further increase the anti-competitive effect of the “no-talk” restriction and further limit the effectiveness of the “fiduciary out”.

With respect to the length of exclusivity arrangements, the Panel referred to the AusNet Services decision which had considered that 8 weeks was at the longer end of market practice. In Virtus’ situation the Panel were concerned that the mechanisms in the Process Deed with respect to the exclusivity period, the diligence period and the end date could mean that some exclusivity arrangements were in place for a number of months. The Panel considered that given that there was only an indicative proposal from CapVest, the duration of the exclusivity arrangements exacerbated the anti-competitive effect of the arrangements.

Virtus submitted that the opportunities of running an auction for control were significantly impaired by virtue of BGH having acquired a 19.99% pre-bid stake and argued that without the Process Deed the Virtus board genuinely believed that CapVest would not have made a proposal. The Panel accepted that sometimes if one bidder had a pre-bid stake, the target might find it more difficult to create an effective auction process. However with two credible bidders in play the Panel saw no intent by Virtus to stimulate competition by, for example, providing feedback to BGH which could have brought forth an improved offer, before entering into the Process Deed.

The orders, and what happened next

The Panel ordered that the no-talk, no due diligence, fiduciary carve-out, non-public information and notification obligation cease to be effective from 8 pm on the 2nd business day after the Panel’s orders unless the Process Deed was amended in a form acceptable to the Panel to deal with these matters. Virtus and CapVest were also prohibited from entering into any binding agreement and CapVest was prohibited from announcing a takeover bid for a period up until ten business days after an announcement by Virtus to the effect that it had amended the Process Deed or that the relevant clauses were no longer in effect.

On 24 February 2022 Virtus announced changes to the Process Deed which:

- removed the delay affecting the “fiduciary out”;

- did not require Virtus to disclose information that would be commercially sensitive information of a third party; and
- excused Virtus from notifying a competing proposal until after its Board had determined whether there was a genuine competing proposal in play.

Key takeaways

In Guidance Note 7 the Panel provides guidance on a number of mechanisms used by bidders to “lock-up” the target to deal with them in priority to others, and emphasises that the Panel will consider substance over form. The Virtus decision illustrates how the Panel will consider such mechanisms, and emphasises that the “fiduciary out” should provide a genuine opportunity for target boards to consider credible alternative bids.

[1] Reasons for Decision Virtus Health Limited [2022] ATP 5

[2] A “fiduciary out” allows the target board to breach exclusivity if the target receives an unsolicited proposal which is superior to the initial proposal. In such circumstances, the target’s directors’ fiduciary duties require them to evaluate the superior proposal, consistent with their duty to act in the best interests of shareholders.

[3] Takeovers Panel Guidance Note 7 “Lock-up devices”

https://www.takeovers.gov.au/content/DisplayDoc.aspx?doc=guidance_notes/current/007.htm&pageID=&Year=