

UK PUBLIC M&A UPDATE

Changes to the UK Takeover Code in relation to asset valuations

1 April 2019

On 6 March 2019, the UK Takeover Panel (the “Panel”) published Response Statement 2018/1 (the “RS”), which confirmed that the amendments to the UK Takeover Code (the “Code”) in relation to asset valuations proposed by the Panel in Public Consultation Paper 2018/1 will take effect on 1 April 2019, with certain minor modifications. In this Alert Memorandum we summarize the forthcoming changes to Rule 29 and the key points to note for Code companies and their advisers.

BACKGROUND

The principle underlying Rule 29 of Takeover Code is that asset valuations given in relation to a target or securities exchange bidder in the context of a takeover bid are of such fundamental importance to target shareholders in their evaluation of the merits of the bid that they should have the benefit of an opinion on the valuation from an independent, competent valuer. Rule 29 of the Code prescribes when such opinions are required, what those opinions must contain and which valuers are permitted to give them.

Asset valuations were published by targets in the following recent UK takeover bids: *DNO ASA’s* (successful, hostile) bid for *Faroe Petroleum plc* and the (subsequently abandoned) bid for *Intu Properties plc* by a consortium comprising, among others, *The Peel Group and The Olayan Group*.

From October to December 2018, the Panel consulted on proposed changes to Rule 29. The new Rule 29 is intended to codify existing practice in this area which is not reflected in the current Rule 29; provide clarity in relation to certain aspects of the requirements; and ensure that asset valuations made in the course of an offer are supported by a valuation report in a proportionate and logical way.

The Panel received responses to its public consultation paper from nine respondents, including investment bodies and the Law Society. As a result of the responses, the Panel has decided to adopt the proposed amendments, subject to certain limited modifications.

The new Rule 29 will take effect on 1 April 2019, including in relation to on-going transactions which straddle that date (except where that would give the amendments retroactive effect). Therefore, if parties have any concern as to how the rule changes may affect them, their advisers should consult the Panel as soon as possible.

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The full text of Response Statement 2018/1 can be accessed via this [link](#).

The full text of Public Consultation Paper 2018/1 can be accessed via this [link](#).

The full text of the Takeover Code can be accessed via this [link](#).

THE CHANGES

The new Rule 29 largely retains the same concepts and requirements of the current Rule 29 with certain additions and clarifications. Unless otherwise stated, references below to rules are to the new Rule 29 as set out in the RS.

Rule 29.1: Applicable valuations

Rule 29 applies to valuations published (i) during the offer period; (ii) within the 12 months prior to the start of offer period; or (iii) more than 12 months prior to the start of the offer period *if* the bidder or target draws attention to the valuation in the context of the bid. However, Rule 29 does not apply to a valuation published by a cash bidder in respect of assets of that cash bidder. The Panel also has discretion to grant dispensations for valuations that the Panel considers not to be material to target shareholders in assessing the merits of a bid ([Rule 29.1\(a\)](#)). As to what types of valuation will be considered not to be material to target shareholders, the RS clarifies that advisers should consult the Panel on a case-by-case basis, as this will depend on the particular circumstances.

Types of Asset. Rule 29 applies by default to valuations of (i) land, buildings, plant or equipment; (ii) mineral, oil or gas reserves (although not volume quantifications of reserves alone, without a value being stated); and (iii) unquoted investments representing in aggregate 10% or more of the gross asset value of the party to the offer which published the valuation ([Rule 29.1\(b\)](#)). Moreover, the Panel has discretion to apply Rule 29 to valuations of other assets or liabilities that would be material to target shareholders in evaluating the merits of the bid, *e.g.*, pension fund surpluses or deficits ([Rule 29.1\(c\)](#)).

Note that an “*illustration of value*” (*i.e.*, where a company seeks to show that if, for example, a particular division were to be valued on the same EBITDA multiple as its market competitors, it would be worth a specified amount) will not usually be subject to the requirements of Rule 29 (but will remain subject to the requirements of Rule 19.1 (*Standards of care*)).

Net Asset Values. Where a securities exchange bidder or a target publishes, or has published, a Net Asset Value or Adjusted Net Asset Value (NAV) in circumstances where Rule 29 would apply if a valuation had been published in respect of the underlying assets, it must also publish a valuation of the underlying assets and set out any adjustments made in the valuation to allow target shareholders to reconcile any differences between the underlying assets and the NAV ([Rule 29.1\(d\)](#)).

Note that Rule 29 is *not* intended to apply to a valuation which is set out in a company’s financial statements only as a result of accounting practice and which is not otherwise referred to by the relevant party in the arguments as to the merits or demerits of the offer ([Note on Rule 29.1](#)).

Rule 29.2: Requirement for valuation report

Any valuations published during the offer period must be in the form of, or accompanied by, a valuation report ([Rule 29.2\(a\)](#)).

Valuations published before the offer period must either be confirmed or updated with a valuation report which will be circulated with the offer document or defence document (as the case may be) or, if earlier, in the first announcement or first document that refers to the valuation ([Rule 29.2\(b\)](#)).

Valuation reports must be prepared by a valuer that satisfies the requirements of Rule 29.3 ([Rule 29.2\(c\)](#)).

Consistent with current practice, where a target or a securities exchange bidder which has published a valuation prior to the commencement of the offer period is unable to obtain a valuation report within the timeframe set out in Rule 29.2(b), the Panel may consent to a delay in the publication of a valuation report, but will only consent to a delay beyond the date of the offer document or defence document (as the case may be) in exceptional circumstances ([Note on Rule 29.2](#)).

Rule 29.3: The valuer

[Rule 29.3](#) sets out the requirements which a valuer appointed under Rule 29 must satisfy and removes the emphasis on property valuations and property valuation practices in the current Rule 29.

A valuer must: (i) be independent to the parties of the offer (for which, see below); (ii) be appropriately qualified to conduct the valuation (with membership of a professional body being an indicator that a valuer is appropriately qualified); and (iii) have sufficient current knowledge of the relevant market and the necessary skills and understanding to prepare the valuation report (*Rule 29.3(a)*). The Panel must be consulted in advance if there are any doubts as to whether a proposed valuer satisfies these requirements (*Rule 29.3(b)*).

For the purposes of determining whether a valuer is independent, the Executive has traditionally applied a lower bar than that applied to financial advisers that wish to be regarded as independent for the purposes of Rule 3.1. The Executive will usually consider a valuer to be independent if: (i) neither the valuer nor any party to the offer has a substantial economic interest in the other; and (ii) the valuer is considered by its own professional standards to be independent and/or is not in breach of its own professional standards by carrying out the valuation. The Panel has affirmed this approach in relation to *Rule 29.3*.

Rule 29.4: The valuation report

The new *Rule 29.4* will combine and refine the requirements currently set out in Rules 29.2, 29.4 and 29.5.

A valuation report must contain: (i) details of the valuer (name, address, professional qualifications); (ii) date of valuation; (iii) details of assets subject to valuation; (iv) separate valuations of each category or each significant asset(s), consistent with any previous published valuations or normal valuation reporting practices; (v) details of the valuations standards relied on; and (vi) the basis of valuation (*Rule 29.4(a)*). The valuation report must also be published on a website in manner compliant with the Code (*Rule 29.4(d)*).

A valuation report must not be qualified or subject to special assumptions (e.g., an assumption which would not be made by a typical market participant in a transaction on the date of valuation) (*Rule 29.4(b)*), and must be published on a website in accordance with Rule 26.3.

A valuation must normally be carried out in respect of all of the assets in a portfolio, but, where the portfolio

contains a large number of similar assets and the valuer is familiar with the portfolio as a whole, the Panel may permit a valuation of a representative sample of each asset class instead (*Rule 29.4(c)*). In such cases, the valuer must report on the representative sample and certify the representative nature of the sample, and the directors must take sole responsibility for estimates, based on the sample, to cover the remaining properties (*Note 4 on Rule 29.4*).

A valuation report must be prepared in accordance with: (i) valuation standards published by the Royal Institution of Chartered Surveyors or the International Valuation Standards Council; or (ii) other appropriate professional standards approved by the Panel, and in each case on a basis which is consistent with past practice in relation to the assets concerned (*Note 1 on Rule 29.4*). The basis of valuation should normally be market value (*Note 2 on Rule 29.4*).

Additional requirements apply to the valuation of land that is being developed or with immediate development potential (*Note 3 on Rule 29.4*).

Rule 29.5: No material difference statement

If the valuation was carried out before the date of the document or announcement in which the valuation report is published, the directors will have to state that the valuer has confirmed that an updated valuation would not be materially different (*Rule 29.5(a)*). If that statement cannot be made, an updated valuation must be published (*Rule 29.5(b)*).

Rule 29.6: Potential tax liability

The new *Rule 29.6* will retain the existing requirement that a valuation report must include a statement as to the tax consequences of a sale of assets, but also codifies the Executive's usual practice of requiring that statement to include an estimate of the amount of tax liability that would arise from the sale. A comment on the likelihood of any such liability crystallizing must also be included (*Rule 29.6(a)*).

Where the Panel has consented to an estimate being omitted, the document or announcement must explain why an estimate cannot be given and describe (in

qualitative terms) the tax consequences of a sale (*Rule 29.6(b)*).

Rule 29.7: Profit forecasts

Rule 29.7 is a new requirement to consult the Panel in advance if a valuation contains a profit forecast under Rule 28 (e.g., where industry practice is to set out detailed projections of the revenue and cost cash flows used to derive the valuation). This is most relevant to oil and gas companies, where valuation reports have, in the past, included numbers which, taken together, constituted a profit forecast.

Rule 29.8: Valuation of another party's assets

Rule 29.8 retains the existing rule (currently contained in Rule 29.1(d)) that a party to an offer will not normally be permitted to publish a valuation of the assets of another party to an offer unless the valuation is the subject of an unqualified valuation report prepared in accordance with Rule 29 by a valuer who has had access to sufficient information to prepare such a report.

However, the Panel is removing the language currently in Rule 29.1(d) that provides that comments by one party about another party's valuation, appraisal or calculation of worth of its own assets may be permitted in exceptional circumstances. The Panel's rationale for removing this language is: (i) subject to Rule 19.1 (*Standards of care*), the Code should not restrict one party's ability to critique an asset valuation published by another party; and (ii) a requirement to consult the Panel might imply that the Panel has pre-vetted the comment, which is unlikely to be the case.

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