ALERT MEMORANDUM

UK TAKEOVER CODE UPDATE

Panel publishes Response Statement 2017/1: Asset Sales and Other Matters

13 December 2017

On 12 July 2017, the UK Takeover Panel published Panel Consultation Paper 2017/1 (the PCP), which proposed amendments to the UK Takeover Code in relation to asset sales by a target company in competition with, or as an alternative to, a takeover offer (and certain other miscellaneous amendments). On 11 December 2017, the Panel published Response Statement 2017/1 (the RS) having received responses to the PCP from eight respondents, including the Association for Financial Markets in Europe, the Quoted Companies Alliance and the Joint Working Party of the Company Law Committees of the City of London Law Society and the Law Society of England and Wales. The RS summarizes the responses received by the Panel and sets out the changes to the Code that will take effect on 8 January 2018 (including in relation to ongoing bids).

If you have any questions concerning the changes to the Code, please reach out to your regular firm contact or to:

LONDON

Simon Jay
+44 207 614 2316
sjay@cgsh.com

Michael McDonald
+44 207 614 2290
msmcdonals@cgsh.com

Tihir Sarkar
+44 207 614 2205
tsarkar@cgsh.com

Sam Bagot
+44 207 614 2232
sbagot@cgsh.com

Mike Preston
+44 207 614 2255
mpreston@cgsh.com

Nallini Puri
+44 207 614 2289
npuri@cgsh.com

Matt Hamilton-Foyn
+44 207 614 2361
mhamilton-foyn@cgsh.com

The full text of the PCP can be accessed via this link and the RS via this link.

Our alert memorandum on the PCP can be accessed via this link.

The full text of the Takeover Code can be accessed via this link.

BACKGROUND

The bulk of the PCP set out the Panel's proposals to amend the rules of the Code in order to address situations in which a target proposes a sale of its assets in competition with or as an alternative to a takeover bid. These proposals were in large part a reaction to two transactions that took place in 2016 (*Harbourvest's bid for SVG Capital* and *Constellation Software's bid for Bond International Software*), which highlighted (in the case of *SVG Capital*) the availability of asset sales as a means by which bidders and targets might circumvent the Code restrictions that apply following a "no increase" statement and (in the case of *Bond International*) the potential advantages that a recommended asset purchaser might enjoy versus a hostile takeover bidder as a result of the application of the Code to takeover bids, but not generally to asset sales.

Most of the proposals in the PCP are being adopted without substantial amendment. However, the Panel has decided to make a small number of changes to reflect concerns raised by respondents, including to increase the threshold test for the Panel to apply certain rules of the Code to asset transactions in competition with a takeover bid.

ASSET SALES

Background

A *"no increase" statement* is a statement by a bidder that it will not increase its offer price above the current price, or that its current price is "final". When a bidder makes a "no increase" statement, it is restricted under the Code from increasing its bid and, if its bid fails, from announcing a new bid within three months, even with the approval of the target board (other than in certain limited circumstances). However, the Code does not currently restrict a bidder that has made a "no increase" statement from agreeing with the target board, after its takeover bid has lapsed, to acquire all or substantially all of the target's assets at a "see-through" price above the takeover bid price (*i.e.*, a price that will result in a distribution to target shareholders at a price per share above the bid price).

A "*Rule 2.8* statement" is a statement that a named person does not intend to make a bid for a Code company. Rule 2.8 statements are typically made following a leak of a person's interest in a potential bid (if the Panel requires an announcement), or after an earlier possible offer announcement (a so-called "*Rule 2.4* announcement") that names the potential bidder and commences the 28-day put up or shut up period under *Rule 2.6* in respect of that bidder. A person that makes a Rule 2.8 statement is restricted under the Code from announcing a bid for the target (and from taking certain other actions) for a period of six months, but is not currently restricted from purchasing all of the assets of the target as an alternative to a takeover bid during that six-month period.

Similarly, the Panel has historically taken a somewhat hands-off approach in relation to asset transactions competing with a takeover bid, only taking jurisdiction over competing takeover bids for the target's shares and (to a limited extent) other transactions that might frustrate an ongoing bid or possible bid. The result is that, where a hostile bidder faces off against a recommended asset purchaser, the asset purchaser has fewer regulatory hurdles to clear and, as such, has a distinct advantage (*e.g.*, the Code does not currently require the target board to publish independent advice on the financial terms of the asset transaction, unlike for the takeover bid).

"No increase" statements and Rule 2.8 statements

With effect from 8 January 2018, a takeover bidder will not be able to circumvent the Code restrictions that apply following a "no increase" statement or a Rule 2.8 statement, by purchasing (or announcing an intention to purchase) *assets that are significant in relation to the target* as an alternative to its bid (including for a

designated period after its bid has lapsed or been withdrawn). For these purposes, significance will be assessed using consideration, assets and profits ratios with a threshold of **75%** (rather than the 50% threshold proposed in the PCP). The rules affected are *Rule 2.5(a)* (*Terms in possible offer announcements*), *Rule 2.8* (*Statements of no intention to bid*), *Rule 12.2* (*Competition reference periods*), *Rule 32.2* (*No increase statements*) and *Rule 35.1* (*Delay of 12 months*).

In Appendix C to the RS, the Panel has summarised how the restrictions will operate in practice following a Rule 2.8 statement or a "no increase" statement.

Frustrating action

The rules that restrict a target board from taking action that could frustrate a takeover bid, including implementing an asset disposal as an alternative to the bid (*Rule 21.1*), are being amended, including:

— to require the target board to publish the substance of independent advice on the financial terms of any competing transaction (*e.g.*, an asset sale). This is notwithstanding that a majority of the respondents to the PCP considered that this requirement was unnecessary and/or duplicative of existing requirements under the Code or the Listing Rules and/or disproportionately burdensome; and

— to require the target board to publish a circular to its shareholders (where approval is being sought for the competing transaction) or make an announcement (where approval is not being sought because the competing transaction is conditional on the takeover bid lapsing), in each case containing specified information regarding the competing transaction. The RS states that, where the target makes an announcement rather than publishing a circular, the Panel is likely to require the announcement to be sent to shareholders anyway.

Quantified financial benefits statements and price-setting

The *quantified financial benefits statements (QFBS)* regime in the Code is being expanded so that, where, *as an alternative to a takeover bid*, the target board announces an intention to sell *all or substantially all of the target's assets* and return to shareholders all or substantially all of the target's cash balances, any statement by the target board quantifying the cash sum expected to be returned to shareholders will be treated as a QFBS (and must therefore be prepared in accordance with *Rule 28* and supported by statements from the target's financial adviser and reporting accountants).

A *new Rule 4.7* is also being introduced into the Code to restrict a recommended asset purchaser from acquiring target shares during a competing bid, unless the target board has publicly announced the cash sum expected to be returned to target shareholders as a result of the asset purchase in accordance with Rule 28 (and only then at prices *below* the per-share equivalent of that sum). The RS clarifies that, where the target board has announced a range of possible cash amounts, the bottom of the range will set the ceiling price for share purchases by the asset purchaser.

Disclosure of information to bidders in competition with asset purchasers

The rules requiring a target board to treat competing bidders equally (in terms of diligence information) (*Rule 21.3*) are being expanded so that, if, *during a bid or after the point at which the target board suspects that a bid might be imminent*, the target board commences discussions with a potential purchaser of *all or substantially all of the target's assets*, any diligence information given to that potential asset purchaser must be given, on request, to each takeover bidder or bona fide potential takeover bidder.

The RS has clarified that:

— the Code will not impose an obligation on the target to provide any information to potential asset purchasers (only competing takeover bidders); and

— the obligation will not apply to any information given to a potential asset purchaser (whether before or after a potential takeover bidder emerges) if the target was already in discussions with the potential asset purchaser prior to the point at which the target board had reason to believe that a takeover bid might be imminent.

OTHER MATTERS

Setting aside a Rule 2.8 statement

Although a person that makes a Rule 2.8 statement is restricted under the Code from announcing a bid for the target (and from taking certain other actions) for a period of six months, these restrictions fall away automatically in certain circumstances (*e.g.*, if the target consents or if a third party announces a bid).

From 8 January 2018, the restrictions on the bidder will only fall away if, in the Rule 2.8 statement itself, the bidder has *expressly* reserved the right to set aside the statement in certain circumstances and those circumstances have materialized. The list of circumstances that a bidder will be permitted to include in its Rule 2.8 statement mirror the circumstances that currently cause the statement to fall away automatically.

The Panel has included two example Rule 2.8 statements in Appendix D to the RS – one including reservation language that can be used if the Rule 2.8 statement is being made at a time where no other bidder has announced a firm offer for the target and the other including reservation language that can be used if another bidder has already announced a firm offer for the target.

Social media

In September 2016, the Panel updated the Code to regulate more explicitly the use of social media by bidders and targets during the course of a bid. However, in the PCP, the Panel acknowledged that its changes might be excessive insofar as they applied to ordinary course, non-bid-related communications by bidders and targets via social media such as Twitter and Facebook. Therefore, with effect from 8 January 2018, the restrictions in *Rule 20.4* will only apply to information about the bid (not the parties to the bid). Rule 20.4 will also be amended to make it clear that the parties to a bid may use social media to post videos relating to the bid that have already been approved by the Panel and published in accordance with *Rule 20.3*.

Rule 19.1 will also be amended to make it explicit that financial advisers are responsible for guiding their clients – *and their clients' PR advisers* – regarding information published on social media during a bid.

"Accelerated whitewashes"

On 8 January 2018, the Panel's practice of granting "accelerated whitewashes" will be codified. An accelerated whitewash is a dispensation from the *Rule 9* mandatory offer requirement where, as a result of an issuance of new securities in a Code company, a subscriber's holding of voting rights would increase through 30% (or between 30% and 50%), provided that independent shareholders holding more than 50% of the votes capable of being cast on a whitewash resolution at a general meeting (*i.e.*, a resolution to waive the mandatory bid requirement) confirm in writing that they would vote in favour of such a resolution if it were put to them.

The accelerated whitewash procedure is particularly useful for smaller Code companies for whom the cost of a formal whitewash procedure could be disproportionate to the value of the relevant transaction.

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