

The UK Takeover Code: Significant Changes Come Into Effect

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On 19 September, a number of changes to the City Code on Takeovers and Mergers (the City Code), the regime that governs public company takeovers and similar transactions affecting the control of public companies in the United Kingdom (takeover transactions), came into effect. The changes, which are being introduced following a series of public consultations, are designed to address a perceived imbalance in certain aspects of the existing regime in favour of potential bidders, and are likely to have a significant effect on the way public company takeovers are approached in the UK. In particular, they are likely to impact the tactics adopted by potential bidders at the outset of any proposed takeover transaction. The changes will affect a number of areas of bid practice.

Virtual Bids

In recent years, an increasingly common tactic has been the use of the “virtual bid,” under which a potential bidder announces that it is considering making an offer (thereby placing the target in an “offer period”), but does not commit itself to do so. The Takeover Panel (the Panel) has expressed concern that such virtual bids have been used to keep potential targets under market pressure for prolonged periods, with little attendant pressure on the potential bidder. Under the new regime, the following will occur:

- Where an announcement is made about a possible bid, the target will be obliged to name all of the potential bidders with which the target is then in talks. However, if a further bidder subsequently enters into talks, there is no obligation for its name to be disclosed (unless it is the subject of rumour/speculation).
- Under a significant tightening of the PUSU (put up or shut up) regime, once a potential bidder is named, it will have 28 days to formally commit itself to make a bid by making a “firm intention” announcement or to announce that it will not make a bid (thereby debaring it from making a bid for the target for six months, except in certain circumstances).
- The revised City Code also formalises the unwritten rule that a potential bidder need not be named in an announcement if the Panel is satisfied that it has withdrawn from bid talks with the target. However, in such circumstances, such potential bidder will be debarred from making an offer for the target for six months, except in certain circumstances.

In effect, these changes impose a 28-day limit on any bidder to complete any pre-bid due diligence and other bid preparations (including having committed bid financing in place) from the time of any initial announcement. Given that a bidder may not be able to control the timing of any initial announcement (for example, in the event of leaks relating to it or any other potential bidder), the new rules could have significant implications for the timing of the initial approach by a potential bidder to the target, and for the likelihood of a potential bidder proceeding with an offer. The 28-day deadline can be extended, with the Panel's consent, if the target board requests this, but this request can only be made shortly before the deadline expires. In addition, the deadline will fall away for all potential bidders once any bidder has made a "firm intention" announcement, although a later deadline, usually "Day 50" of the bid timetable, will then apply for clarification by all named potential bidders of their intentions. In addition, the deadline will not apply if the target board has formally announced that the target is up for sale.

Deal Protection Measures

In recent years, the range and extent of deal protection measures sought by potential bidders as a precondition to proceeding with an offer have grown considerably. The Panel had become concerned that these measures were becoming seen as market standard, rather than heavily negotiated on a case-by-case basis, and were being used to deter other potential bidders. The revised City Code now heavily regulates the use of deal protection measures, and many previously permitted measures are now prohibited:

- All "offer-related arrangements" (which is broadly defined) are now prohibited, except for a narrow category of permitted measures or with the consent of the Panel.
- In particular, break fees (or inducement fees) are now prohibited, although these may be permitted where an alternative "white knight" bidder approaches the target in a hostile bid situation, or where a target company has put itself up for sale.
- Other prohibited measures include "no shop" undertakings, matching and topping rights, and undertakings not to provide information to other potential bidders.
- Permitted measures include confidentiality agreements; commitments to provide information to assist in obtaining regulatory and other clearances; covenants not to solicit employees, customers, or suppliers; commitments to accept an offer; any measures binding a bidder (except where the deal is a reverse takeover); and existing employee-incentive arrangements.
- Provisions regulating the conduct of schemes of arrangement are also prohibited. However, if a takeover transaction is to be implemented by way of a scheme where the takeover transaction is recommended, the target will be obliged to publish the scheme timetable in the target circular, and the target will be required to implement the scheme in accordance with that timetable unless certain circumstances arise, including a withdrawal of the recommendation. A bidder will also be able to withdraw its offer if certain key dates in the scheme timetable are not met if the bidder has included offer conditions to this effect.

Increased Disclosure of Offer-Related Matters

The revised City Code requires disclosure of information in a number of new areas:

- Both the bidder and target will be required to provide a detailed breakdown of advisory fees by category of adviser, including financing fees.
- Bidders are required to include financial information, even in the context of a cash bid.
- Bidders will be required to disclose more extensive details of any bid financing arrangements, including the amount of each facility, repayment terms, interest rates (including any “step up” provisions), security provided, key covenants, and the identities of the principal lenders.

Bidder’s Intentions

The revised City Code contains new provisions designed to improve the quality of disclosure by a bidder as to its intentions for the target post-offer in relation to the target’s employees, business locations, and fixed assets, as well as the continuation of any market quotation for the target’s shares. In particular, negative statements are now required if there are no plans. A bid party will be bound by any public statement made on such matters, either for the time specified in the statement or for 12 months, unless there is a material change in circumstances.

Other Key Changes

A considerable number of other changes to the City Code have been made, ranging from the substantive to the clarificatory. The following are two of the other key changes:

- The rights of employees and employee representatives to be informed about, and comment on, any offer have been strengthened.
- The City Code expressly states that the target board is not limited by the City Code in the factors it may consider in deciding whether to recommend an offer, and in particular that the City Code does not require the target board to treat price as the determining factor.

Transitional arrangements apply where offer periods commenced before 19 September.

Given the significance of these changes and the likelihood that they will affect bid practice, the Panel has indicated that it intends to review how they are operating in practice 12 months after their implementation, subject to there be sufficient bid activity. Following representations made during the consultation process, the Panel has also indicated that it intends to consider whether to consult on possible further changes to the City Code to grant information and opinion rights (similar to those currently granted to employee representatives) to pension fund trustees.

If you have any questions or would like more information on the issues discussed in this LawFlash, please contact the following Morgan Lewis attorney:

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