Feature

**KEY POINTS**

- The Takeover Code is now far more complex than it has ever been.
- Circumstantial evidence suggests the so-called Cadbury law and the 2011 amendments have not damped takeover activity.
- The role of lawyers in advising on and ensuring compliance by clients with the Takeover Code has arguably eclipsed that of the bankers in many respects.

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## All change at the ToP: taking stock of the changing nature of the UK takeover regime

In 2011, following Kraft Food’s takeover of Cadbury the Takeover Panel introduced a number of amendments to the Takeover Code with the aims of redressing the balance of power in favour of target boards, of ensuring that greater account is taken of the views of persons affected by takeovers in addition to target shareholders (such as employees) and of increasing transparency. The Kraft/Cadbury offer, and a number of subsequent large offers, also prompted a debate about government intervention in takeovers, including whether governments should be able to apply national interest tests to foreign takeovers of companies involved in certain sectors of importance to the UK economy. Concern was expressed that the 2011 amendments to the Takeover Code and political interference, which many felt played a larger part in prompting the Takeover Panel to make the amendments, would impede takeover activity. This article considers the impact of some of those amendments and how the Takeover Code and the role of the Takeover Panel have evolved in recent years as a result of various factors, such as the increasing global nature, size and sophistication of takeovers, political intervention, and increased scrutiny and regulation of financial markets in the aftermath of the financial crisis.

### INTRODUCTION

The takeover of Cadbury plc by Kraft Foods Inc (Kraft), which commenced in early 2010 prompted widespread public discussion about the regulation of UK takeovers. Cadbury was subject to a long virtual bid process. Many commentators argued that it was too easy for an unsolicited offeror to subject an offeree company to a protracted siege which could be destabilising for the offeree and its business and employees, and that the outcomes of takeovers, particularly hostile offers, were unduly influenced by the actions of “short term” investors. On 1 June 2010, the Code Committee (Code Committee) of the Takeover Panel (Panel) commenced a public consultation on suggested amendments to the Takeover Code to address these concerns. The Code Committee’s response statement noted “significant conflicts of views” on some of the proposed amendments.

The Code Committee ultimately decided to implement several of the proposed amendments, with the key aims of:

- redressing the balance of power in favour of offeree companies;
- ensuring that greater account was taken of the position of persons affected by takeovers in addition to offeree company shareholders, most notably employees; and
- increasing transparency and improving the quality of disclosure.

### KEY 2011 AMENDMENTS

#### Naming of potential offerors and compulsory PUSU

One of the most hotly debated amendments at the time was the introduction of a requirement for any announcement by an offeree of an approach or possible offer to name the potential offeror(s) with which it was in talks or from whom it had received an approach. Another was a requirement that any named potential offeror must, except with Panel consent, within 28 days following the announcement in which it was named (PUSU deadline), announce either a firm intention to make an offer or that it would not make an offer, in which case it would, subject to exceptions, be locked out from announcing an offer for the target for up to six months. The Panel generally grants an extension to the PUSU deadline only if requested by the target company. The purpose of these amendments was to avoid protracted and destabilising virtual bids for target companies.

When the Panel consulted on these proposed amendments, two thirds of respondents opposed the identification rule arguing that it would deter potential offerors who would not wish to be named prematurely and, if the offer did not proceed, be associated with a failed transaction. The majority of respondents were concerned that 28 days was too short a period to allow for adequate preparation for an announcement of a firm intention to make an offer. In both cases, the respondents who objected were concerned that legitimate potential offerors might be deterred and that shareholders might consequently be denied the opportunity to consider valid potential offers.

#### Prohibition of “offer-related arrangements”

“Offer-related arrangements” such as inducement/break fees, non-solicitation undertakings and matching rights granted by an offeree in favour of an offeror were outlawed, except in certain very limited circumstances. These sorts of deal protection measures had become commonplace and the Code Committee wished to reduce the tactical advantages obtained by the offeror imposing complex arrangements that tied target boards in knots but which they felt compelled to accept.

This proposal received either support or a neutral response from roughly two thirds of the respondents to the consultation. The concern of the remaining third was, similarly, that this rule would deter potential offerors, in particular private equity bidders, from...
making offers, again to the detriment of the shareholders of target company shareholders.

STATEMENTS REGARDING THE EMPLOYEES AND BUSINESS OF THE OFFEREED

Offerers have for many years been obliged to disclose their intentions regarding the commercial rationale for an offer, their strategic plans for the business of the offeree, and their plans for the offeree’s employees and fixed assets. In 2011 a rule was introduced to the effect that a bidder would be expected to comply with such intention statements for 12 months from the end of the offer period or such other time as was specified by the bidder, unless there was a material change of circumstances. This rule was largely uncontroversial with approximately two thirds of respondents approving of it.

The new rule was supplemented in January 2015 following statements by Pfizer and AbbVie in the course of their attempted takeovers of AstraZeneca and Shire respectively about their plans for the respective target companies’ UK operations, in particular their R&D operations. A bifurcated approach was introduced which distinguished between “post-offer undertakings” and “post-offer intention statements”.

A post-offer undertaking is a commitment by a party to an offer to take or not to take a course of action after the end of an offer period. Any such commitment must be approved by the Panel before it is made and it is then subject to detailed regulation under the Takeover Code, including post-closing compliance monitoring. Bidders have so far been wary of giving such commitments and practitioners expect them to be very much the exception rather than the rule.

A post-offer intention statement is a statement by a party to an offer that it intends to take or not to take a particular course of action. It must be an accurate statement of that party’s intention at the time the statement is made and be made on reasonable grounds. If a party wishes to depart from its stated intention within 12 months from the end of the offer period, the Panel must be consulted.

ENHANCED DISCLOSURE REQUIREMENTS

Since 2011, offer documents must contain additional information on the offeror’s bid financing and any facilities which will be used to refinance the offeror’s existing indebtedness, including repayment terms, interest rates, maturity dates and key covenants, and the relevant debt documents must be put on display.

Both the offeror and the offeree must disclose their estimated fees in connection with the offer by category, including financial, legal, accounting and PR, and make supplementary disclosures if the actual fees in any category exceed the estimate by 10% or more.

In order to allow employee representatives and pension scheme trustees the opportunity to form and disclose their views on a bid, offeree boards must inform them at the earliest opportunity of their right to circulate an opinion on the effects of the offer on employment and pensions respectively. The offeree is responsible for publishing and paying for the opinion(s).

IMPACT OF THE AMENDMENTS HAVE THE AMENDMENTS TO THE TAKEOVER CODE DAMPENED TAKEOVER ACTIVITY IN THE UK?

There is no definitive answer to this question, but circumstantial evidence would suggest that the amendments discussed above have not dampened activity. According to the annual statistics published by the Panel, there was, between 2011 and 2014, a steady decline in the number of offeree companies which went into an offer period. In the 12 months to 31 March 2011, 134 offeree companies went into an offer period. There were 61 in 2014. However, this decline is more likely to be down to market factors rather than the amendments to the Takeover Code and this is reinforced by: (i) the fact that the decline commenced after 2007 (the last peak of the M&A market); and (ii) the increase in the number of offer periods to 89 in 2015 (a 46% increase over 2014). Interestingly, 2015 showed a significant increase in the total value of announced takeovers and in the number of larger deals compared to 2011: 2015 saw 14 deals announced with a value of £1bn or more, compared to 3 in 2011, and 33 with a value of £100m or more, compared to 21 in 2011. Of note are the recent mega-deals: Shell’s £47bn offer for BG Group in April 2015 and AB InBev’s proposed £71.24bn offer for SAB Miller, which is the highest value offer to date for a UK company.

Of particular concern when the 2011 amendments were introduced was that private equity bidders would be deterred by their inability to use break fees to hedge their costs on aborted deals, by the requirement for potential bidders to be named in announcements, by the time pressure of the PUSU deadline, and by the extended financial disclosure requirements.

... there is a feeling among some PEs that the 2011 amendments have made the UK a more difficult environment in which to make public offers.
been to make potential bidders more attentive to the need to preserve confidentiality in advance of announcing an offer and to be better prepared at an earlier stage of the process. Parties are also adapting to the stricter regime. An example of this is a topping insurance product offered by Aon in response to the prohibition on break fees and which provides cover for costs incurred if a bidder is defeated by an interloper.

- a growing proportion of extremely large offers and attempted offers, such as AB InBev’s £71.24bn offer of SAB Miller, Pfizer’s attempted £69bn offer for AstraZeneca, and AbbVie’s attempted £27bn offer for Shire, which, because of their size and the fact that they were unsolicited, attracted significant publicity and put the Panel and the Takeover Code under the public spotlight; and
- the growing sophistication in the way deals are executed, in part due to increasing globalisation and the involvement of large foreign participants.

The Panel has also had to cope with considerable political and government intervention in public takeovers, most notably during and following the Kraft/Cadbury, Pfizer/AstraZeneca and AbbVie/Shire transactions, all of which were originally unsolicited and involved foreign bidders. There is some debate about the impact which political and government intervention at the time of these high profile transactions had on the Panel’s decision to amend the Takeover Code. Many members of parliament and ministers believed that these transactions illustrated the vulnerability of UK companies to hostile or predatory foreign takeovers. They expressed concern about the effect which foreign takeovers of major British companies would have on employment and on Britain’s manufacturing and R&D base, and about the allegedly detrimental influence of short term investors, many of whom were foreign, on the outcome of takeovers.

All three of the proposals mentioned above provoked debate in parliament and the media about whether a public interest test should apply to attempted foreign takeovers in certain sectors considered key to the British economy, such as the pharmaceutical sector. With so much attention focused on its rules, the Panel could not avoid acting.

The consequence of these factors is that the Takeover Code is now far more complex than it has ever been. Its size has increased exponentially in recent years and there are significantly more steps and compliance requirements involved in the offer process. The tone of the Takeover Code has also changed: as it has become more complex, it has also become more legalistic in nature, notwithstanding that it is famously not drafted as statute. The corollary is that the role of lawyers in advising on and ensuring compliance by clients with the Takeover Code has arguably eclipsed that of the bankers in many respects...

**CHANGING ROLE OF THE PANEL**

Although the 2011 amendments do not appear to have had a significant impact on M&A activity, what has been changing is the complexity and breadth of the Code. This is largely due to a number of challenges which the Panel has had to face since the start of the millennium and the rapidly developing nature of takeovers. These challenges have included:

- the growing use of derivatives and other similar instruments;
- more intense scrutiny of financial markets and a far more complex regulatory environment in the aftermath of the financial crisis;
- the increasingly global nature of M&A, with more foreign bidders for UK companies (foreign bidders were responsible for 8 of the 10 largest deals in the first half of 2015 at the time of writing of this article, three of the largest offers being contemplated for UK companies involve foreign offerors: AB InBev for SAB Miller; Deutsche Boerse for London Stock Exchange; Steinhoff for Home Retail Group) and the resulting need for the Panel to take into account the interaction, and occasional conflict, between the Takeover Code and foreign regulatory requirements;
- notwithstanding that it is famously not drafted as statute.

The UK takeover regime is admired around the world for its fairness and transparency, and for the Panel’s pragmatic approach, and its ability to act swiftly and adapt to change. It is likely that the pace of change which we have seen over the past few years will continue unabated as transactions become larger and more sophisticated and global in nature. It is also likely that, as global capital and business interests continue to collide with local political and fiscal interests, governments and politicians will continue to intervene in larger takeovers. All of this means that there might yet be a lot more change to come for the Panel.

1 The Code Committee received comments on the consultation questions from 57 respondents.
2 Source: LexisNexis, part of LexisPSL Corporate.