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# In Practice

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## How committed is a 'Committed Facility'? – issues to look out for when reviewing a credit facility for the purpose of providing a cash confirmation statement

In order to provide the certainty of funding required by General Principle 5 of the City Code on Takeovers and Mergers, certain modifications need to be made to a credit facility. This article examines those modifications.

### THE REQUIREMENT FOR A CASH CONFIRMATION

General Principle 5 of the City Code on Takeovers and Mergers (the 'Code') requires that an offeror must announce a bid only after ensuring that it can fulfil in full any cash consideration. Accordingly, under rules 2.5(c) and 24.7 of the Code, when an offer is for cash or includes an element of cash, both the press release and the offer document must include confirmation by the bidder's financial adviser that sufficient resources are available to the bidder to satisfy full acceptance of the offer. The financial adviser giving the cash confirmation will not be expected to produce the cash itself, if, in giving the confirmation, it acted responsibly and took all reasonable steps to assure itself that the cash was available.

Consequently, financial advisers need to take seriously their responsibility to assure themselves, before the press release announcing the offer is issued, that the bidder will have the cash it needs to implement the offer in full. As part of that process, the financial adviser will need to review carefully any credit facility that is being relied on by the bidder to fund its offer.

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### THE CERTAIN FUNDS PERIOD

In order to provide the certainty of funding required, the provisions in the credit facility relating to conditions precedent, events of default, representations and warranties and undertakings will need to be modified for the so-called 'Certain Funds Period'.

The length of the Certain Funds Period is not set in stone and is often keenly negotiated. Ideally, it should last sufficiently long to enable the bidder to satisfy its payment obligations under the offer and under the compulsory acquisition procedures of s 429 of the Companies Act (approximately seven months from the announcement of the offer as a rule of thumb).

In some cases, lenders may be uncomfortable with that length of Certain Funds Period. From the point of view of the Code, the Certain

### KEY POINTS

- As a minimum, the Certain Funds Period should cover the period of the offer timetable.
- Only specified defaults will act as drawstops to loans to be used to fund the offer.
- Conditions precedent must be satisfied at the time of execution of the credit facility or, provided they are within the control of the bidder, soon thereafter.
- Market flex clauses that allow lenders to make changes in pricing should be acceptable for cash confirmation purposes.
- A practice is developing whereby offers are announced on the basis of an interim funding agreement.

Funds Period is not required to cover the time required to complete the s 429 compulsory acquisition procedures. Accordingly, as a minimum, the Certain Funds Period should cover the period of the offer timetable. This should amount to the aggregate of:

- 28 days from the offer announcement for posting the offer document;
- a further 60 days for the offer to become unconditional as to acceptances;
- a further 21 days for any remaining conditions to be satisfied;
- and a further 14 days for the consideration to be satisfied.

This totals approximately four months. However, a Certain Funds Period this short would allow a bidder little flexibility to pursue its offer if a competitive situation were to arise and, as a consequence, the offer timetable had to be extended.

### CERTAIN FUNDS DEFAULTS

Bidders and their financial advisers will want to limit as far as possible during the Certain Funds Period any conditionality of the provision of the financing under the acquisition facility.

Accordingly, during the Certain Funds Period, bidders and their financial advisers will want to ensure that the standard 'no default' and 'no material misrepresentation' drawstops are disapplied and will want only specified defaults ('Certain Funds Defaults') to act as drawstops to loans to be used to fund the offer.

Although there is no right or wrong approach and each deal will depend on the relative bargaining positions of the parties, typically these will include:

- Non-payment under a finance document.
- Breach of the negative pledge, the disposals undertaking or the

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offer-related covenants. Sometimes breaches of other covenants will be included as Certain Funds Defaults – for example, breach of the restriction on acquisitions, borrowings or guarantees; breach of the covenant regarding the application of equity, debt or disposal proceeds, or breach of the covenant restricting ownership of target shares. In considering these, the key for the bidder and its financial adviser will be to ensure that they are all matters that the bidder is able to control.

- Breach of representations as to legal matters, but only in relation to the original obligors.
- The insolvency and insolvency proceedings events of default – but usually only in relation to the original obligors.
- The unlawfulness and repudiation events of default.

Bidders and their financial advisers should also check whether the credit facility covers the following points:

- restriction on cancelling the facility (with exceptions for illegality or if certain offer-related events occur – such as a competition reference);
- acceleration being restricted to the occurrence of Certain Funds Defaults; and
- suspension of the 'change of control' mandatory prepayment event.

## CONDITIONS PRECEDENT

Bidders and their financial advisers will want to ensure that conditions precedent have either been satisfied at the time of execution of the credit facility or that there is no doubt that they will in due course be able to be satisfied (because, for example, they are within the control of the bidder). Thus, the forms of all certificates, legal opinions etc will need to be agreed on signing of the credit facility and, so far as possible, any such documents should be available for delivery. Confirmation should be obtained from the lenders as to which conditions precedent have been satisfied and which remain to be satisfied. Conditions that cannot be satisfied need to be within the control of the bidder. For example, a condition precedent that the offer document is delivered to the lenders would be acceptable, provided that (for example) it does not have to be 'in form and substance satisfactory' to the lenders. A no-material adverse change condition would not be acceptable.

## MARKET FLEX CLAUSES

Any offer by a lender to provide debt financing to fund an offer will typically be subject to a 'market flex' clause. Market flex clauses are usually contained in the mandate letter, rather than the credit facility, but will normally remain effective even after the credit facility is signed. Market flex clauses are designed to protect the lenders underwriting the offer, financing against subsequent difficulties in syndicating the financing.

Market flex clauses take many forms: some allow the lenders to propose changes to the structure, terms and/or pricing (but not the amount) of the financing at any time before completion of syndication. Others allow a change to the pricing only.

A market flex that only provides for a change in pricing should be acceptable for cash confirmation purposes but a market flex that allows for changes to structure or pricing is unlikely to be acceptable, since changes made to the structure or terms could take away the certainty of funding.

## TIMING

A formal cash confirmation statement is required from the moment that the press release announcing the offer is made and so it is at this point that the financial adviser must be able to satisfy itself as to the certainty of the funds available to finance the offer. Thus, it will be essential that the credit facility is signed, and conditions precedent to drawdown have been satisfied, before announcement.

In exceptional circumstances, bidders and their financial advisers may allow an offer to be announced on the basis of a binding underwriting letter for the required amount of financing accompanied by a detailed term sheet.

Given the uncertainty and risks associated with announcing an offer on the basis of a term sheet, a practice in the market has recently developed of announcing an offer on the basis of an interim funding agreement. This would be a fully committed facility agreement with the representations, covenants and events of default being limited to those that would ordinarily apply during the certain funds period. The interim funding agreement will usually have a term extending a few weeks beyond the certain funds period and will usually be subject to a higher margin in order to encourage a prompt refinancing. It will then be replaced by a fully documented credit facility containing the full set of representations, covenants and events of default that will apply beyond the Certain Funds Period.

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Although this is seen as a useful tool in giving parties the opportunity to negotiate the full-form credit facility in a more relaxed timeframe, lenders will often want to have the full-form credit facility in place prior to the offer document being posted to shareholders. At that point, all material contracts (of which the credit facility will be one) are required to be put on display and lenders' usual preference is to have the full-form credit facility rather than the interim agreement on display.

In switching between the interim funding agreement and the full-form credit facility, bidders and their financial advisers will need to ensure that the same degree of certainty of funds as existed immediately prior to announcement of the offer is preserved. ■