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Corporate M&A

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UK

LAW & PRACTICE: p.3

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The 'Law & Practice' sections provide easily accessible information on navigating the legal system when conducting business in the jurisdiction. Leading lawyers explain local law and practice at key transactional stages and for crucial aspects of doing business.

Contributed by Travers Smith LLP **Authors:** *Richard Spedding, Spencer Summerfield, Philip Cheveley, Andrew Gillen*

Law & Practice

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Travers Smith LLP is an international law firm operating from a City of London hub. The firm is widely seen as a market leader and regularly wins awards for its M&A skills, acting on all types of domestic and cross-border transactions in both the public and private fields. The practice consists of a 90-plus strong team of M&A lawyers advising on a full range of deal structures from public takeovers and buy-outs to divestments, demergers and joint ventures. M&A is supported by the corporate finance practice which delivers equity fundraisings with an in-house US securities law capability. The team also has integrated support from the financial services and markets practice, tax, operational risk team, commercial and acquisition finance.

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1. Trends

1.1 M&A Market

As predicted, 2015 was a record-breaking year with M&A targeting the UK up 193% (by value). Investor confidence, strong balance sheets and an encouraging domestic environment enabled the UK to play a pivotal role with a share of nearly 40% of European M&A activity. 2015 saw five record-breaking deals worth over GBP10 billion, the highest in a decade, and there was a 50% increase in GBP1+ billion deals over 2014. Anheuser-Busch InBev's GBP79.6 billion acquisition of SABMiller, the largest deal by value globally, and Royal Dutch Shell's GBP47 billion acquisition of BG Group in third place contributed to the record-breaking deal activity.

Private Equity activity remained a strong element of M&A activity in 2015. Private Equity firms increasingly sought to divest to corporates, consequently trade sales reached an all-time high (68.6% increase by value compared to 2014).

North American based firms featured heavily in targeting UK-based assets (99 transactions worth GBP23.7 billion).

The full-year forecast for 2016 is harder to call, tempered by continued uncertainty over China's slowdown, commodity price uncertainties and the upcoming US presidential election. The fundamentals for M&A still hold good, however, and Q1 2016 volumes for cross-border M&A on a global level are up against Q1 2015.

In the UK, the EU referendum has cast an additional shadow of uncertainty over 2016 with Q1 deal activity down nearly 50% compared to Q1 2015. This in turn reduced the UK's market share of European M&A activity to 22% for the quarter. Inbound and outbound deal activity dropped by 35% and 44.6% respectively. Outbound activity suffered its lowest deal count since Q1 2013, possibly impacted by a fall in the relative value of sterling to reflect the referendum outcome.

The uncertainty created by the "Brexit" decision will provide volatility for some time to come. We think it likely that the FX movements in GBP will give buying power to overseas-domiciled corporates and financial sponsors, leading to opportunistic inbound M&A.

1.2 Key Trends

Like the US, the UK has been host to a number of mega-deals over the last 18 months, with the highlight of Q1 2016 being the GBP10.5 billion merger talks between the London Stock Exchange and Deutsche Boerse. A consequence of such deals is the greater likelihood of regulatory barriers, which in turn leads to a greater number of public bids being subject to preconditions and drawn-out timetables. The UK Takeover Panel has brought in provisions facilitating the use of 'clean teams' in the diligence process, illustrating the prevalence of regulatory sensitivities. There are also signs of regulators flexing their muscles (eg the CMA intervention in the Hutchison/O2 merger) and being less willing to approve deals without a committed buyer in place for merger control divestments.

The UK offers an attractive regime for overseas buyers, where regulators rarely intervene in blocking merger activity unless there are anti-trust or national security concerns. Political calls for a broader national interest test to protect so-called "national treasures" seem to have dissipated – at least for the moment. The UK has over the last 18 months also been a jurisdiction of choice for US companies seeking tax inversions, but the collapse of the Pfizer/Allergan merger may have been the high water mark on such deals – thanks in this case to the US Treasury.

In contrast, PLC-on-PLC activity has fallen away relatively – only 27% of 2015 bids were wholly domestic. Interestingly, we have seen an uptick in private equity-backed bids, having been subdued for a few years. This is no doubt in part due to the huge amount of "dry powder" that private equity managers have at their fingertips, with pressure to deploy. Whereas we have seen sustained sell-side activity by private equity funds in 2015, we see 2016 as being more balanced, both in the public and private buyout markets. Anecdotally, the strictures of the UK Takeover Code set in 2011 had a negative influence on the private equity industry, but private equity bidders may now have become more accustomed to the landscape and the lack of cost coverage and deal certainty they can get from the target. To assist further, we see signs of an insurance solution to the lack of target break fees.

Another noticeable trend has been the greater advent of alternative sources of debt finance, used particularly by non-trade buyers (for example, Cerberus financing GVC's bid for bwin.party).

1.3 Key Industries

The Consumer, Energy, Mining and Utilities sectors topped the tables in 2015, with deals worth GBP89.7 billion and GBP57.8 billion respectively. Consumer deal value saw an increase of more than eleven times when compared with 2014 due to Anheuser-Busch InBev's GBP79.6 billion acquisition of SABMiller.

Low oil prices are expected to drive medium-term deal activity in 2016, with possible consolidation in the Energy, Mining and Utilities sectors. Financial Services was the most active sector by value in Q1, but this was skewed by the GBP10.5 billion merger talks between London Stock Exchange (LSE) and Deutsche Boerse. Increased activity in the Telecommunications, Media and Technology sector is also expected. Fintech remains a particular hotspot in London, with rapidly growing companies attracting strong valuations and seeking growth capital or even access to the public markets.

2. Overview of Regulatory Field

2.1 Acquiring a Company

Acquisitions of UK companies almost invariably take place through the transfer of shares in the target: the UK does not have an effective regime for statutory mergers whereby one UK entity can merge into another, and regulations facilitating cross-border mergers between UK and other EU entities are rarely used in practice. Instead, the mechanisms used tend to be a function of whether the deal is a private M&A transaction or a public takeover.

A private M&A acquisition is usually structured as a purchase of shares in the target or of business and assets owned by the seller(s) pursuant to a sale and purchase agreement. A share purchase involves the buyer acquiring all of the target's assets and liabilities through buying the target legal entity, even if these are unknown. By contrast, a business purchase involves the buyer acquiring individual, specific assets and liabilities which are usually clearly identified in the transaction documents. The general principle of UK asset deals is that the buyer does not take on any assets and liabilities unless they are expressly specified in the transaction documents; but there are exceptions to this (for example, the transfer of employment liabilities – see **2.5 Labour Law Regulations** below).

A public takeover involves the acquisition of control of a target, either by a contractual offer or by a court-approved scheme of arrangement. Unlike private M&A, where all sellers participate (or have their shares acquired by contractual drag-along provisions), public takeovers are structured to make use of mechanisms to enable the acquisition of minority shareholder interests. Public M&A involving a UK PLC is

almost invariably governed by the City Code on Takeovers and Mergers (the **"Code"**).

In a contractual takeover offer, a bidder makes an offer directly to target shareholders to tender their shares. If the bidder receives acceptances in respect of at least 90% of the target's shares (excluding those which it already owns) it can compulsorily acquire (or "squeeze out") minority shareholders. A takeover will be either a voluntary or mandatory offer. A voluntary offer is one that the bidder chooses to launch having assessed the commercial benefits and potential synergies of the proposed enlarged group. A mandatory offer is required by the Code when a bidder has acquired at least 30% of the voting rights in the target, or where, already holding between 30% and 50%, it acquires additional interests in target shares. Voluntary and mandatory offers may be either recommended (ie supported by the directors of the target) or hostile.

In contrast to a contractual offer, a scheme of arrangement is a statutory procedure whereby the target enters into an arrangement with its members which requires the court's sanction to become effective. Typically, the arrangement is a transfer of target shares in consideration for shares and/or cash in the bidder. The scheme binds all shareholders if it is approved by a majority of shareholders voting (in person or by proxy), holding at least 75% by value of the shares voted. It is sanctioned by the court and registered with the Registrar of Companies.

Schemes are a popular takeover structure. They achieve 100% control more quickly than contractual offers and, depending on the composition of the share register, may be the more effective means of acquiring 100%. Their popularity continues even though the ancillary benefit of avoiding a 0.5% stamp duty charge has recently been removed. However, in practice, schemes cannot be used for hostile offers or mandatory offers.

2.2 Primary Regulators

The Takeover Panel is the regulator of public takeovers in the UK and the UK's designated authority to supervise takeover bids for the purposes of the EU Takeover Directive. Its role, through the application of the Code, is to provide an orderly framework for takeovers and to promote the integrity of the financial markets in conjunction with other regulatory regimes. It is not concerned with the financial merits or commercial terms of a particular transaction, nor with questions of public interest, such as competition policy, which are the responsibility of government and other bodies.

The Panel has a series of powers and duties under the Companies Act 2006. These include powers to give a direction to restrain a breach of the rules of the Code, secure compliance with them, or apply for court enforcement; to require documents or information for the exercise of its functions; and to impose sanctions. In performing its functions, it is required to co-operate (including sharing information, where it is not prevented from doing so) with the Financial Conduct Authority ("**FCA**"), the Prudential Regulation Authority and the Bank of England.

The FCA is the UK's financial services regulator responsible for conduct and market regulation and regulating issuers and major shareholders subject to the listing regime. However, the FCA will generally not intervene in a takeover situation unless the Panel's powers are insufficient to address any market abuse element and it has requested the FCA to use its enforcement powers.

Similarly, the Panel has a duty to co-operate with foreign regulators which fulfil equivalent functions. It is also under the authority of the European Commission, both directly through the Takeover Directive and also through the EC Merger Regulation, which controls merger and acquisitions activity in the EU, raising antitrust concerns.

The Competition and Markets Authority ("**CMA**") is the UK authority with jurisdiction over antitrust matters.

Although decisions of the Panel have historically been found to be subject to judicial review, in Re Expro International Group Plc, the court commented that it is not appropriate for the court procedure involved in a scheme to allow an undesirable level of uncertainty, which the provisions of the Code have successfully reduced or eliminated in the case of contractual offers. Accordingly, it appears unlikely that the courts will play a more active role in determining the outcome of takeover offers.

2.3 Restrictions on Foreign Investment

There is no specific legal regime which governs foreign investment in the UK. In certain limited situations, the UK government may be able to intervene in a merger, albeit these situations are not solely confined to cases of foreign inward investment. An example under the Enterprise Act 2002 arises when a proposed merger may give rise to issues of national security (see **2.6 National Security Review** below) or other defined public interest issues. In some regulated industries in the UK, regulatory or governmental consents may be needed to effect an M&A transaction, such as broadcasting, financial services and utilities.

2.4 Antitrust Regulations

A corporate M&A transaction in the UK may require merger control clearance from the CMA and/or competition authorities in other jurisdictions, depending on whether certain thresholds are met.

Merger control thresholds vary across jurisdictions, but are typically based on an assessment of the parties' turnover generated from sales to that jurisdiction, asset values, and/or market shares. Asset purchases, acquisitions of minority shareholdings and joint ventures may also require merger control clearance depending on the jurisdiction.

For a transaction involving parties with very significant worldwide turnover, or where the parties generate turnover across a range of EU Member States, the financial thresholds set out in the EC Merger Regulation ("**ECMR**") may be met. If so, the European Commission will have exclusive jurisdiction to review that transaction within the EU, although in some cases it is possible that the transaction (or part of it) might be referred back to a national competition authority for review. The transaction must be notified to, and cleared by, the Commission prior to completion. In carrying out its review, the Commission will consider whether the transaction may significantly impede effective competition.

Where a transaction does not meet the ECMR thresholds, it may instead meet the relevant thresholds for review by national competition authorities in the EU, including the CMA. The CMA may review a transaction where either: (a) the UK turnover of the enterprise being acquired exceeds GBP70 million; or (b) it results in a share of 25% or more in the supply of goods or services in the UK as a whole (or a substantial part of it) being created or enhanced. In carrying out its review, the CMA will consider whether the transaction may result in a substantial lessening of competition. This relationship between the ECMR and the UK merger control rules may change in the future depending on the nature of a British exit from the EU.

Unlike under the ECMR, notification in the UK is voluntary, and therefore it is possible to complete a transaction without notifying it to, or receiving prior clearance from, the CMA. However, for some months after completion, the CMA has the power to commence an own-initiative merger control review, and can require that the relevant businesses be held separate from each other during its review. Therefore careful consideration is usually given in UK corporate M&A transactions as to whether the deal should be made conditional on a UK merger control clearance.

Parties to a UK corporate M&A transaction should also bear in mind that where the relevant businesses generate revenue from customers located outside the UK/EU, other national merger control thresholds may be met, and other clearances may therefore be required.

2.5 Labour Law Regulations

Unlike an acquisition of business and assets, a share acquisition will not trigger a duty to inform and consult employee representatives or the automatic transfer of contracts of employment under the Transfer of Undertakings (Protection of Employment) Regulations 2006. There may nonetheless be broader obligations (perhaps under any separate information and consultation agreements) to inform and consult with trade unions or other employee representative bodies (including any works councils that may exist) about a proposed takeover. Furthermore, subsequent business rationalisation measures could trigger a requirement for the relevant employing entity to make redundancies, in turn possibly triggering collective redundancy consultation obligations and exposure to potential liability for employment-related claims, including unfair dismissal.

However, the employee-related provisions of the Code need to be considered closely to implement a successful public takeover. The Code requires disclosure of the bidder's intentions regarding employees and requires information about the offer to be communicated to employees. Any possible offer announcement, the firm offer announcement and the offer document must be readily available to employee representatives or, if there are no employee representatives, to the employees themselves. The rules in the Code supplement any applicable obligations to consult with works councils, but do not themselves create consultation rights.

The Code is designed to help employee representatives be more effective in providing their opinions on the effects of the takeover on employment. The target board must inform them at the earliest opportunity of their right to circulate an opinion on this. It must also make clear that it is the target board's responsibility to publish the opinion (by appending it to the board's circular at the target's expense if received in good time, or via a website and announcement) and the target's responsibility to pay the employee representatives' costs reasonably incurred in obtaining advice to verify information in the opinion (although the opinion itself will not be the target board's responsibility).

The Code also gives trustees of defined benefit pension schemes similar rights to those which apply to employee representatives.

2.6 National Security Review

Irrespective of whether a corporate M&A transaction meets the merger control thresholds noted above, particular issues may arise where the transaction involves the acquisition of a business which is directly or indirectly involved in the provision of goods or services in the defence sector.

In such cases, the Secretary of State for Business, Innovation and Skills can intervene in the transaction, by issuing an intervention notice, if:

- he believes that the deal may raise national security considerations; and

- the merger control thresholds set out at **2.4 Antitrust Regulations** above are not met, then at least one of the parties carries on business in the UK; and
- the deal involves a current or former government contractor who has or has had access to confidential defence-related information.

The issue of an intervention notice triggers a separate statutory procedure which includes an assessment of the national security implications of the transaction.

The intervention notice procedure is rarely used in practice, but it should also be noted that UK Ministry of Defence (**"MoD"**) contractors are usually contractually obliged to notify the MoD of transactions. Generally this notice is given prior to completion in order to give the MoD a sufficient opportunity to consider the potential implications of the transaction from a national security/defence standpoint.

3. Recent Legal Developments

3.1 Significant Court Decisions or Legal Developments

Since 4 March 2015, there has been a prohibition on takeovers by way of a cancellation scheme of arrangement (ie a scheme where all the shares in the target not already owned by the bidder are cancelled by a reduction of capital of the target and the bidder pays the bid price to the target shareholders in consideration for their agreement to cancel their shares). The advantage of a cancellation scheme, as opposed to the alternative – a transfer scheme – used to be that since no shares are transferred, no stamp duty was payable, resulting in a considerable saving of transaction costs. Takeovers by way of a scheme must now be effected by a transfer scheme, where shares in the target not already owned by the bidder are transferred to the bidder and therefore stamp duty is payable on the transfer. There is a carve-out from the prohibition to allow a scheme which amounts to a restructuring that inserts a new holding company into the group structure, provided that all or most of the members of the company become members of the new holding company and their proportionate holdings remain substantially the same.

3.2 Significant Changes to Takeover Law

Post-offer undertakings and statements of intention

In January 2015, in the aftermath of Pfizer's possible offer for AstraZeneca and Kraft's bid for Cadbury, the Panel brought in changes to the Code to strengthen the regulation of promises made by bidders in an attempt to win the bid battle. The Code now distinguishes between undertakings (statements *committing* a bidder to take, or not take, a particular course of action after the offer ends) and statements of intention (statements that a bidder *intends* to take or not take a particular course of action after the offer ends), with stricter requirements applying to the former. The offer document must expressly state where a post-offer undertaking is being made; specify the time for which the undertaking lasts and state prominently any qualifications or conditions to which it is subject. Generic 'material change of circumstances', directors' fiduciary carve-outs and unspecified force majeure events are not permitted.

Treatment of dividends

In November 2015, the Panel brought in changes to the Code relating to the treatment of dividends. Under the revised rules, a bidder can only reduce the bid consideration (should the target company subsequently pay a dividend) if it has reserved the right to do so in its possible bid announcement (Rule 2.4 announcement), any subsequent firm bid announcements (Rule 2.7 announcements) and the offer document.

Offer-related arrangements and equality of information provided to competing bidders

In October 2015, the Panel published two new Practice Statements clarifying its approach in relation to Rule 21.2 (inducement fees and offer-related arrangements) and Rule 21.3 (equality of information to competing bidders).

Firstly, Practice Statement no. 29 sets out the Panel's views on whether certain commitments breach the rules against offer-related arrangements. In relation to directors' irrevocable undertakings, the Panel sets out examples of commitments given in irrevocables from target company directors who are also shareholders, which it considers to be in breach of these rules. These examples include non-solicit and notification undertakings and commitments to recommend a bidder's offer or conduct the target business in a particular manner, even when subject to directors' duties. The Practice Statement also covers other commitments, including commitments to provide information or assistance for the purpose of obtaining any official authorisation or regulatory clearance (eg consent of competition authority); commitments relating to reverse break fees; agreements relating to existing employee incentive arrangements; and bid conduct agreements, in each case giving examples of both what is permitted and what is prohibited under the Code.

Secondly, Practice Statement no. 30 sets out the Panel's view on how the requirements of Rule 21.3 may be complied with where it is necessary to provide a limited amount of commercially sensitive information to certain lawyers or economists advising a bidder on an 'outside counsel-only' basis for the purpose of enabling them to consider the need for the consent of a competition authority or regulatory body. The Panel's practice is normally to agree that the requirements of Rule 21.3 will be satisfied if, upon the restricted information being requested by a competing bidder, it is provided to the anti-trust lawyers or economists advising the competing bidder on the same restricted "outside counsel only" basis.

If this is done, the Panel will not require the restricted information to be provided directly to a competing bidder. In practice, this will only be relevant where two competing bidders have a merger control issue. The restricted information should only be provided to a small number of identified lawyers and economists who are specifically engaged to provide advice to the relevant bidder in relation to the competition or other regulatory aspects only of the offer (the "clean team").

Future changes
Changes to the Takeover Code will take place on 12 September 2016 in relation to the communication and distribution of information and opinions during an offer. Under the revised Code, where material new information or significant new opinions relating to an offer or a party to the offer have been: (a) published; (b) provided to any shareholder (or other person interested in securities) or to any investment manager, investment adviser or investment analyst; or (c) provided to the media, then that information or opinion must be published via a "regulatory information service" or "RIS" announcement (subject to limited exceptions). Presentations or other documents relating to an offer or a party to an offer, and media communications relating to an offer or a party, must be promptly published on a website regardless of whether the relevant document contains any material new information or significant new opinion. There will also be new rules prescribing when videos and social media can be used during an offer, and new rules on meetings held by telephone calls or other electronic media.

4. Stakebuilding

4.1 Principal Stakebuilding Strategies

Stakebuilding is relatively rare in the UK in light of the various hurdles discussed below. When used effectively, however, it can help a bidder improve the chance of its bid succeeding and can deter or block competing bidders. It may also help the bidder defray its bid costs if it is outbid by a rival bidder. A bidder's strategy will be to balance the deterrence advantages against the downsides of upfront funding and the fact that a purchase typically sets the benchmark price for any subsequent offer.

A 10% holding would always be enough to prevent minority squeeze-out in a contractual offer by a rival bidder. A 25% holding would always be enough to block a rival scheme of arrangement. In practice, stakes lower than 10/25% will have a blocking effect, as there is always an element of the share register that does not participate in acceptance/voting. Bidders may choose to use stakebuilding in conjunction with seeking contractual undertakings or statements of intent from other shareholders to support acceptance of their offer or to vote in favour of their scheme (**"irrevocable undertakings"**).

4.2 Material Shareholding Disclosure Thresholds

Two regimes govern the disclosure of shareholdings in a takeover of a UK issuer: the Disclosure Guidance and Transparency Rules (the **"DTRs"**) and Rule 8 of the Code. Under the DTRs, a shareholder in a UK issuer listed in the UK must notify the company within two trading days if the percentage of voting rights it holds through a direct or indirect holding of shares or other financial instruments reaches, exceeds or falls below 3% or any whole percentage figure above 3% (DTR 5). A UK issuer must then make an onward public disclosure within one trading day. The shareholder must also notify the FCA where the disclosure relates to shares traded on a regulated market (eg the Main Market, but not AIM). Different thresholds apply to non-UK issuers.

After an offer period has commenced, additional disclosure requirements are also triggered under Rule 8 of the Code in relation to positions and dealings in securities in the target and (irrespective of its jurisdiction of incorporation or listing) a securities exchange bidder. Relevant securities exclude shares held in treasury.

First, there is an opening disclosure requirement on any person who is interested in 1% or more of any class of relevant securities of the target or of any securities exchange bidder to disclose details of interests and short positions in each company by 3:30 pm on the tenth business day after the offer period commences. Concert parties' positions should be included. The Panel removed in January 2015 the requirement for a bidder to make an immediate opening position disclosure where, at the time of its firm offer announcement, it has not already made an opening position disclosure.

Second, a dealing disclosure is required by any person who is or becomes interested in 1% or more of any class of relevant securities of the target or of any securities exchange bidder if the person deals in any relevant securities of either company. A dealing disclosure must contain details of the dealing concerned and of the person's interests and short positions in any relevant securities of each company by 3:30 pm on the business day following the date of dealing.

Opening position and dealing disclosures must in any event be made by the bidder and target, and dealing disclosures must also be made by each of them and by their concert parties. For these persons there is no 1% threshold: disclosure is required of *all* positions and dealings.

A public company also has a statutory power to investigate its share register by sending notices to persons known or suspected to be interested in shares requiring them to give details of their interest. In a suspected takeover situation, this is an important tool of the target board to establish the true composition of its share register and even informal arrangements among shareholders.

4.3 Hurdles to Stakebuilding

Whilst a company can set out more stringent reporting thresholds in its articles of association than those described in **4.2 Material Shareholding Disclosure Thresholds**, in reality it would not voluntarily take on more rigorous reporting obligations. A company cannot introduce less stringent thresholds.

A number of restrictions apply to stakebuilding. Notably, it could give rise to a criminal offence under insider dealing legislation or a civil offence under the market abuse regime. Generally, stakebuilding is inadvisable if the bidder has received any non-public information about the target through due diligence. At the time of writing, some questions remain as to the application of the Market Abuse Regulations which came into effect in July 2016, but it is generally understood that a bidder can acquire shares in the knowledge only of its intention to make a takeover offer.

A series of restrictions under the Code on dealing in shares of both bidder and target must also be observed in relation to connected persons who hold price-sensitive information. No such person (other than the bidder) who has price-sensitive information in relation to the offer may deal in the target's shares or derivatives between the time when there is reason to suppose that an approach or offer is contemplated and its announcement. The Code also prohibits the bidder and its concert parties from selling any securities in the target during the offer period without the Panel's prior consent.

There are further Code restrictions on a bidder or its concert parties acquiring any interest in shares and/or irrevocable undertakings over 30% or more of the voting rights in the company. Even where this is allowed, a bidder must make a mandatory offer to all outstanding shareholders if it does acquire at least 30% of voting rights or if, already holding between 30% and 50%, it acquires additional interests in shares (although irrevocable undertakings are ignored for this calculation).

If a bidder or its concert parties acquire an interest in shares in the target in the three months before the offer period or between its commencement and its firm offer announcement, a Code offer must be on no less favourable terms. Further, where a bidder and any concert party acquire interests in a target for cash during the offer period or within the 12 months preceding it which carry 10% or more of the voting rights of a class of shares, a cash or cash alternative offer of an at least comparable amount must be made.

Further, in a contractual offer, purchases before an offer document is sent out do not count towards the 90% minority squeeze-out threshold in the UK and, on a scheme, shares already held by the bidder cannot be voted at the court meeting to approve the scheme.

Where the bidder has a premium listing in the UK, there is also a requirement for shareholder approval if the stakebuilding triggers the thresholds for a Class 1 transaction (broadly if the target is at least 25% the size of the bidder on one of a number of metrics).

Finally, if the target is a regulated entity, there may be additional regulatory consents required before a significant stake can be taken. For example, 'controller' approval is required to acquire 10% or more of an entity regulated by the FCA.

4.4 Dealings in Derivatives

Dealings in derivatives are allowed, subject to the same restrictions as share dealings, and fall within the above disclosure obligations under the DTRs and the Code. However, there are market abuse restrictions against a bidder or potential bidder dealing in securities that only give economic exposure to the target share price.

4.5 Filing/Reporting Obligations

Dealings in derivatives are caught by the same DTR and Code disclosure obligations as for shares. The European Market Infrastructure Regulation (EMIR) requires counterparties that fall within its scope (whether financial or non-financial counterparties) to report (to trade repositories) details of over-the-counter and exchange-traded derivative transactions to which they are a party, following the widely drawn meaning of a derivative under the Markets in Financial Instruments Directive (MiFID).

4.6 Transparency

There is no requirement for a stakebuilding bidder to make known the purpose of its share acquisition or its intentions regarding control of the company – and in fact there can be binding or procedural consequences of bid/no bid intention statements. Strictly speaking, it is not until the offer document is despatched that the bidder must disclose its plans for the business, under the requirements in the Code to identify its intentions with regard to the future business of the target and the long-term commercial justification for the offer, as well as its plans for employees and any defined benefit pension scheme. In practice, it is customary for the firm offer announcement to include a short statement in relation to plans for the business and employees of the combined group.

5. Negotiation Phase

5.1 Requirement to Disclose a Deal

A potential bidder must make an announcement when (after it first actively considers an offer but before it makes an approach) the target is the subject of rumour and speculation or there is such a movement in share price and there are reasonable grounds for concluding that it is the potential bidder's actions which have led to the situation. An announcement may also be required when negotiations or dis-

cussions relating to a proposed offer are about to extend to more than a restricted number of people. The Panel should be consulted before more than six parties are approached about an offer or possible offer. Following an approach to the target board, the target instead becomes responsible for making announcements in a number of circumstances set out in Rule 2 of the Code, ranging from when a firm intention to make an offer is notified to the target board to when the target has become subject to rumour and speculation or there is an untoward movement in its share price. Assuming that there are no such triggers, the fact of an approach, letter of intent, due diligence or negotiations does not itself require an announcement. Note, however, that the "PUSU" requirements (discussed in **7.1 Making a Bid Public** below) become relevant if a potential deal is announced.

5.2 Market Practice on Timing

Market practice on the timing of disclosure follows the requirements of the Code, and the Panel would treat failure to comply as a serious breach of the Code – likewise as regards any DTR disclosures.

5.3 Scope of Due Diligence

Due diligence carried out by the bidder on a public takeover is often more limited than on a private acquisition, and the scope varies depending on whether it is a recommended or hostile bid, or made in a competitive situation.

A bidder will inspect publicly available information sources, including information filed with the Registrar of Companies (freely available on the target's website), UK or EU competition law decisions in the relevant business sector and analysts' reports.

The bidder on a proposed recommended offer will generally provide the target with a due diligence request list. The extent of information provided differs considerably depending on the particular circumstances.

Where the target has made information available to one bidder (or potential bidder), it is required to make the same information available on request to all other potential bidders, whether welcome or not. This may mean the target is reluctant to provide information even to a welcome bidder.

Whilst in practice, cash bidders may be given limited due diligence information, more information may be provided if the bidder is issuing shares as consideration for the offer and needs to prepare a prospectus, if needed to assess merger control issues or if the acquisition is otherwise particularly material for it.

5.4 Standstills or Exclusivity

Exclusivity and similar arrangements in a private M&A context are often requested. However, on a public takeover the Code prohibits the target agreeing deal protection measures (broadly defined as "offer-related arrangements"). This catches exclusivity agreements, non-solicitation and break-fee arrangements, all of which are prohibited as a general rule during an offer period or when an offer is reasonably contemplated.

By contrast, standstill agreements impose obligations on the bidder only, and are therefore permitted.

5.5 Definitive Agreements

Terms and conditions of any public takeover will be contained either in a bidder's offer document (on a contractual offer) or in the target's scheme document (on a scheme), and target shareholders will be asked to either accept or reject the contractual offer or vote on the proposed scheme. Rather than signing a definitive document, shareholders will create a contract by signing a form of acceptance on a contractual offer, or will vote on the proposed transaction on a scheme.

6. Structuring

6.1 Length of Process for Acquisition/Sale

A private M&A transaction has no set timetable, being a function only of negotiation and potential third-party clearances. As described above, a public takeover is implemented by either a contractual offer or a scheme, and the overall timetable can end up being much the same for each. On a simple recommended contractual offer, the bidder can obtain control (50.01%) as soon as sufficient shareholders accept the offer, potentially within 21 days of posting the offer document, while obtaining 100% control through a squeeze-out process takes more than nine weeks from posting the offer document. On a scheme, the bidder can obtain 100% control around six to seven weeks after posting the scheme document.

Both a contractual offer and scheme document must normally be posted within 28 days of the firm offer announcement. On a contractual offer, the offer document can be sent on the same day as the firm offer announcement (if it is ready). However, even if the scheme document is ready at the time of the firm offer announcement, it is unlikely it could be sent the same day, due to the requirement to obtain the court's permission to convene the necessary shareholders' meeting.

On a contractual offer, day 21 after the offer document is published is the earliest date on which the offer may lapse if not unconditional as to acceptances (that is, the first possible closing date). An offer must be kept open for 14 days after it becomes unconditional as to acceptances (unless unconditional at the outset). As such, day 35 is the first day the offer may close. Standard practice follows this timing – although it is rare for the acceptance condition to be hit by the first

closing date and the offer is usually extended. The maximum time to meet the acceptance condition is normally 60 days after publication of the offer document. The last day to satisfy all other conditions is 21 days after the later of either the first closing date or the date the offer is declared unconditional as to acceptances (for example, day 81, assuming the offer is unconditional as to acceptances as at day 60). Target shareholders must be paid within 14 days of the offer becoming wholly unconditional.

On a scheme, the timetable is agreed with the court and the scheme could potentially be effective six to seven weeks after posting the scheme document. The shareholder meeting(s) must be held at least 21 days after sending the scheme document (unless the Panel agrees otherwise). Unless there is a competitive bid situation, there is no maximum time limit in a scheme to hold shareholder meetings or satisfy other scheme conditions. On a scheme, there is no equivalent to the 60-day limit for contractual offers.

On a contractual offer, the acquisition of 100% control after the offer has gone unconditional is not certain. Only once the bidder has acquired 90% of the shares to which the offer relates, can it despatch compulsory acquisition notices. The bidder must then wait at least six weeks to acquire 100% control. The earliest possible date would be approximately nine weeks after sending the offer document; however, this would extend to over 15 weeks from sending the offer document if the maximum time to achieve acceptances is required. On a scheme becoming effective, the bidder immediately acquires 100% of the target.

6.2 Mandatory Offer Threshold

Unless the Panel consents otherwise, a bidder for a PLC target must make a mandatory offer under Rule 9 for all existing shares of the target when, together with its concert parties, it acquires an interest in shares carrying 30% or more of the voting rights, or is interested in shares which carry between 30% and 50% of the voting rights and acquires a further interest in shares which increases the percentage of voting rights in which it is interested.

A mandatory offer must be made for cash or accompanied by a cash alternative at not less than the highest price which the bidder or its concert parties paid for shares in the target in the preceding 12 months. It must be conditional only on the bidder and its concert parties reaching 50% acceptances although, where relevant, terms relating to competition references must also be included in the same way as for a voluntary offer (as discussed below).

It is customary for the Panel to waive the requirement for a mandatory offer where the company issues new securities in connection with a subscription for cash or in consideration of an acquisition, provided that the waiver is approved by a vote of independent shareholders (a "whitewash"). Other circumstances in which the Panel will usually waive the requirement, provided that there is such a whitewash resolution, include where a share issue is underwritten. However, the Panel would typically not grant the waiver where new securities are issued to a potential bidder and that bidder or its concert parties has acquired shares in the company in the preceding 12 months.

6.3 Consideration

About 90% of firm offers announced in 2015, and 80% in H1 2016, included cash as the consideration, most often as the sole consideration but sometimes combined with shares, loan notes or unlisted securities. In particular circumstances, the Code stipulates whether cash or shares should be offered as consideration. For example, where the bidder triggers the mandatory offer threshold, a cash or cash alternative offer must be made. Where a bidder and any concert party acquires interests in a target for cash during the offer period or within the 12 months preceding it which carry 10% or more of the voting rights of a class of shares, a cash or cash alternative offer of at least a comparable amount must be made. Where a bidder acquires any interests in a target in exchange for securities of the bidder during the offer period or within the three months preceding it which carry 10% or more of the voting rights of a class of shares, a share offer is normally required to all the holders of the same class, unless the bidder arranges the immediate placing of such consideration securities for cash.

Subject to the above circumstances, there is no general requirement in the Code as to whether cash or shares should be offered as consideration. The identity of the bidder will often be relevant to target shareholders when choosing the consideration. Where it has credible financial records and is well known among investors, target shareholders are likely to be more willing to accept the bidder's shares. However, cash is likely to be more attractive in relation to less well-known public companies or private companies. The shareholder base is also relevant: institutional shareholders are more likely to accept shares, whereas individual shareholders tend to prefer cash.

6.4 Common Conditions for a Takeover Offer

All offers have an acceptance condition, as described below.

Under the Code, a bidder is allowed to include a condition that there is no Phase 2 CMA reference and no European Commission intention to initiate Phase 2 proceedings, in terms satisfactory to it. The Code requires that an offer will lapse if there is a Phase 2 reference to the CMA or if Phase 2 European Commission proceedings are initiated before the first closing date or the date on which the offer becomes or is declared unconditional as to acceptances.

Administrative or procedural conditions are also customary, such as any bidder shareholder approval requirement. However, an offer must not normally be made subject to a financing condition. More broadly, the Code states that an offer must not be subject to conditions dependent on subjective judgements by directors of the bidder or target, or conditions where their fulfilment is within the control of directors of the bidder or target. It also stipulates that Panel consent is required for a bidder to invoke a condition, other than the acceptance condition and a competition condition, and in such cases the circumstances must be of material significance to the bidder in the context of the offer. Whilst a range of other conditions is typically included, such as environmental, industry-related and no material adverse change conditions, the Panel sets the bar on invoking them so high that virtually no bids have ever been given consent to use them.

Separately, the making of the offer can also be subject to preconditions, although this is not standard and the Panel must be consulted first. Without the Panel's consent, the only preconditions which are allowed relate broadly to Phase 2 competition references or, in the case of a recommended bid, other material authorisations or regulatory clearances – typically because conclusion of those matters is not feasible within the Code timetable. The requirements as to no subjectivity and material significance apply equally to preconditions.

6.5 Minimum Acceptance Conditions

Contractual offers must be conditional on the bidder obtaining acceptances in respect of shares carrying more than 50% of the voting rights in the target, the threshold to change the board and otherwise pass ordinary resolutions under English company law. Accepting shareholders take up the offer by completing individual forms of acceptance (or electronic acceptance through the CREST system); they do not become party to an overarching document.

Notwithstanding this minimum level, it is common for the bidder to make any voluntary contractual offer conditional on receiving acceptances in respect of 90% of the shares to which the offer relates in order to ensure that the statutory squeeze-out procedures will be available. This condition is included on the basis that the bidder can waive it down to the minimum 50.01% threshold (which it might wish to do if the deal becomes competitive).

By contrast to a contractual offer, a scheme binds *all* shareholders if it is: (a) approved by a majority in number of shareholders, representing at least 75% in value of the shares of members, voting in person or by proxy; (b) sanctioned by the court; (c) registered with the Registrar of Companies.

6.6 Requirement to Obtain Financing

It is a key principle of the Code that the bidder should announce a firm intention to make an offer only if it has sufficient resources to satisfy full acceptance. The Code states that a bid must not be made subject to a condition or (save as referenced below) precondition relating to financing. In practice, this means that financing agreements must be fully negotiated and signed before the offer is made, and the conditions to drawdown should be satisfied (or, if not capable of being satisfied at that point in time, in agreed form and within the bidder's control) when the offer is announced.

Where cash consideration will be raised by an issue of new securities, the offer will be made conditional on the corporate and regulatory authorisations required to issue such securities, and will ensure they are admitted to trading, but *not* upon any underwriting otherwise becoming unconditional.

The bidder must consult the Panel in advance if it intends to include any precondition to which the posting of the offer will be subject. If a precondition results in an extended period before the offer, the Panel may allow a financing precondition where it is not possible for the bidder to obtain committed financing during the length of time before the offer (for example, due to a requirement to obtain regulatory or other material authorisation).

Where the offer is fully or partly for cash, the Code requires the bidder's financial adviser to make a "cash confirmation" statement in the firm offer announcement and offer document that the necessary funds are available to satisfy full acceptance of the offer. In practice, therefore, the bidder's financial adviser will scrutinise the terms of any financing documents to ensure they meet the "certain funds" requirements of the Code.

6.7 Types of Deal Security Measures

As noted above, deal protection measures have been prohibited since 2011, except with the Panel's consent. This is due to concerns that they may deter competing bidders or prompt them to offer less favourable terms than they would otherwise have done. The types of arrangement caught by the prohibition include inducement fees, undertakings to notify the bidder of competing approaches, matching rights allowing the bidder to match or improve on a competing offer, and exclusivity provisions.

In very limited circumstances the Panel will consent to an inducement fee. Firstly, where a hostile bidder has made a firm offer announcement, the Panel will normally allow such an arrangement between the target and a competing "white knight" bidder, or with a selected preferred bidder at the conclusion of a public auction process for the target. However, in practice this has not been used. Secondly, in a formal sale process (ie where a company announces it is

putting itself up for sale), the Panel may grant a dispensation from the prohibition on break fees. Even in these limited circumstances, the inducement fee must not be greater than 1% of the value of the target and should not be payable until an offer becomes or is declared wholly unconditional.

The Code also provides certain limited exceptions for other arrangements which would otherwise be caught by the prohibition, including confidentiality undertakings, irrevocable undertakings, provision of information to obtain regulatory approvals and undertakings preventing solicitation of employees, customers or suppliers.

6.8 Additional Governance Rights

As a practical matter, the bidder will rarely launch an offer unless it is confident it can secure control of the target; however, the Code permits partial offers. A contractual offer may not be declared unconditional until the bidder has obtained more than 50% of the voting rights in the target.

Aside from the voting rights that accrue to the bidder at shareholding levels of more than 50% and of 75%, being the thresholds for passing ordinary and special resolutions respectively, its opportunities to secure additional governance rights are limited. A minority shareholding of more than 25% affords the ability to block special resolutions. A supportive major shareholder with a shareholding of 20% or more may sometimes seek a seat on the company's board, but has no right to one. Any other additional rights or protections would need to be built into the target's articles of association.

There may be other implications from acquiring less than 100%. The Listing Rules require controlling shareholders (shareholders who, when combined with their concert parties, control 30% or more of votes) to enter into an agreement including required independence provisions with a premium listed company.

6.9 Voting by Proxy

The Companies Act 2006 permits shareholders to appoint a proxy to attend, vote or speak on their behalf at any general meeting. This overrides any contrary provision in the target's articles of association.

In a contractual offer, target shareholders are normally asked to respond to the offer using a form of acceptance enclosed along with the offer document, rather than vote on a shareholder resolution.

On a scheme, or where for some reason a general meeting of the target is required (for example, to approve a special deal with management), the practice is to enclose a form of proxy with the notice of meeting for completion and have it returned by shareholders no later than 48 hours before the meeting (or later, if the articles so provide). It is usual for companies to provide that shareholders can appoint the chairman of the meeting as proxy.

An alternative is for a corporate shareholder to appoint a corporate representative. Institutional shareholders often hold their shares in nominee companies, which tend to rely on corporate representatives rather than proxies, as these may sometimes afford greater flexibility, such as when the deadline for appointing proxies cannot be met.

6.10 Squeeze-Out Mechanisms

A bidder using a contractual offer has a statutory right compulsorily to acquire minority shareholders, provided that it has made a takeover offer for the entire share capital or relevant class of share capital of the target and has secured acceptances in respect of 90% of the shares and voting rights to which the offer relates. The compulsory acquisition must be on the same terms as the original offer, and must, in the case of a company with shares admitted to trading on the Main Market, be notified no later than three months from the last day for accepting the offer. In other cases, such as a bid for an AIM company, the relevant period is six months from the date of the offer if this period is shorter.

Shares which the bidder already holds or has unconditionally contracted to acquire before the offer are not included within the 90% calculation. Target shares subsequently acquire and those subject to irrevocable undertakings to accept the offer may count towards the 90% threshold, provided certain conditions are met.

There is a statutory right for a dissenting minority shareholder to apply to court to contest either the compulsory acquisition or its terms. There is a limited chance of success in these cases. Previous case law indicates that the court operates a presumption that an offer accepted by 90% of shareholders is fair and will not seek to re-examine the merits of the offer except in extraordinary circumstances.

Minority shareholders also have a corresponding right to be bought out on the same basis, if for some reason the bidder does not initiate squeeze-out.

These compulsory acquisition procedures are not relevant in the context of a scheme, where the bidder secures 100% control of the target.

Rule 35.3 of the Code sets out restrictions on a bidder who has taken control of a company making subsequent offers to any remaining minority shareholders. The bidder is restricted, for six months from the closure of any previous offer, from making a second offer or acquiring any interest in shares in the company on more favourable terms than those made available under the previous offer.

6.11 Irrevocable Commitments

It is common for a bidder to seek irrevocables from key target shareholders and (in a recommended bid) from target directors who are shareholders. Under the Code, a commitment to vote in favour of a scheme is considered to be equivalent to an irrevocable commitment.

A bidder will normally approach institutional shareholders to seek irrevocable undertakings shortly before making the firm intention announcement, in most cases the night before or even on the day of the announcement. The Panel must be consulted if any individual or small corporate shareholders are to be approached, and all shareholders must be given sufficient time and information to consider the proposal and come to an informed decision. The Panel must in any event be consulted if more than a very restricted number of people (typically six) are to be approached without making an announcement.

The terms of any irrevocable undertaking are a matter for negotiation between bidder and shareholder. Irrevocables may be "hard", meaning they are binding in all circumstances. Alternatively, irrevocables may be "soft", meaning they lapse in certain circumstances, for example on a competing higher offer, or "semi-hard", meaning they cease to bind if a higher offer or one exceeding a set amount emerges. Most institutional shareholders have policies with regard to irrevocables, for example only to give soft irrevocables or a non-binding indication of their position (a "letter of intent").

Irrevocables and letters of intent must be publicly disclosed by announcement on a website. Irrevocables or letters of intent procured before an offer period commences must be publicly disclosed on the business day following commencement of the offer period or, in the case of a bidder, the date of the announcement first identifying it as the bidder. The disclosure must also include any outstanding conditions to which the irrevocable is subject.

Whilst undertakings given by directors as shareholders are acceptable (such as to accept the offer, vote for the scheme or return proxy forms within a set time), undertakings in the capacity of director are not (such as non-solicitation, recommendation of the bid or convening board meetings to implement the bid).

7. Disclosure

7.1 Making a Bid Public

The Code requires strict secrecy before an offer or possible offer is publicly announced (Rule 2). Financial advisers to bidders have specified responsibilities to warn clients of the importance of secrecy and security. When discussing and documenting a possible offer, code names should always be used.

Information in relation to a possible offer must only be shared on a need-to-know basis and the recipient must always be made aware of the requirement for secrecy. The Panel must be consulted before more than six external parties (finance providers, target shareholders, customers, suppliers etc, but excluding immediate advisers) are approached about an offer or possible offer.

The Code contains provisions governing when and how offers are announced. An announcement is required where negotiations or discussions relating to a possible offer are to be extended beyond the above restricted need-to-know basis, in certain circumstances: if the target is the subject of rumour and speculation or there is an untoward movement in its share price (ie there is a leak) and when a firm intention to make an offer is notified to the target board. Before an approach is made to a target, the onus is on the bidder, after it first actively considers an offer, to make an announcement if the target is subject to rumour, speculation or untoward movement in share price and it is reasonably likely that the bidder's actions are the cause. After an approach, the onus shifts to the target.

Whether an announcement is required is a judgement for the Panel, so parties should consult the Panel as required, particularly where there is rumour or speculation or an untoward movement in share price. A rise of 10% or more above the lowest share price since a potential bidder's approach (or 5% in one day) would be considered material for these purposes. Following a rumour, speculation or untoward movement in share price, the Panel may grant a dispensation from the requirement for an announcement if it is satisfied that the bidder has ceased to actively consider an offer (in which case the bidder will be prevented from doing so for up to six months).

Any announcement by a target triggering an offer period must identify potential bidders with which the target is in talks or from which it has received an approach which has not been unequivocally rejected. Any named bidder must then clarify its intentions, either by making a firm offer announcement or by confirming it will not be making an offer by no later than 5:00 pm on the 28th day after the announcement in which it was first identified, or any extended deadline. In essence, the bidder has to 'put up or shut up' (hence this is known as the PUSU regime). Where a bidder has ruled itself out, it cannot make an offer, or trigger a mandatory offer, for the target for six months. Where another bidder has already made, or subsequently makes (before the end of the 28-day deadline), a firm offer announcement, the PUSU restrictions cease to apply.

7.2 Types of Disclosure

The Code contains an obligation on the bidder to disclose sufficient information to target shareholders to allow them

to reach a properly informed decision with respect to the offer. This should be provided in good time and no relevant information should be withheld. In addition, documents and announcements published in connection with an offer must be made available to the parties' employee representatives and the target's pension trustees.

As discussed above, there are detailed requirements on content to be disclosed in the announcement of an offer and in the offer or scheme document as well as other information to be disclosed and transaction documents to go on display. There are also disclosure requirements on the target to circulate a board circular following publication of the offer document if the target board's view is not included in the offer document, as well as putting certain documents on display.

All content disclosed whether by bidder or target is subject to the highest standards of care and accuracy and fair and adequate presentation. It is the directors' responsibility to ensure the required standards are met. All documentation published in connection with a bid must contain a directors' responsibility statement that the directors accept responsibility for the published information and confirm that it is complete and accurate to the best of their knowledge and belief (having taken all reasonable care to ensure that such is the case).

Where a bidder proposes to offer shares as consideration, it may in certain circumstances need to publish a prospectus or equivalent document. The offer document must also contain a full description of the rights attaching to the shares and (where the bidder is listed) the middle market quotations for the first business days in each of the preceding six months or (where the bidder securities are not listed) an independent valuation of the shares and information on any transactions in them taking place in the previous six months. It must also contain details of the conditions relating to the admission to listing or trading of the consideration shares, which must be in a form approved by the Panel.

7.3 Requirement for Financial Statements

Bidders who are incorporated under the Companies Act 2006 and whose shares are admitted to trading on a UK regulated market or on AIM or ISDX Growth Market must disclose consolidated audited financial statements for the two most recent financial years, along with any interim statements or preliminary announcements made since the date of the last filed audited financial statements. These may be incorporated by reference by providing details of any website address where they have been published.

In addition, where bidder shares are offered as consideration, the bidder must disclose any known significant change in its financial or trading position since the end of the financial period for which audited or interim financial information has been published, or provide an appropriate negative statement.

There is no requirement for pro forma information, but there are additional procedures to be followed in the context of profit forecasts or merger benefits statements.

7.4 Disclosure of the Transaction Documents

A range of documents have to be disclosed on a website. Following a firm offer announcement, documents which must be published on a website include irrevocables, documents relating to financing of the offer, any offer-related arrangements and any agreement with respect to when a bidder might seek to invoke a condition or precondition to its offer. Following an offer, documents which must be published on a website include consents of the financial adviser, material contracts connected to the offer and certain documents in relation to profit forecasts, quantified financial benefits statements and asset valuations.

8. Duties of Directors

8.1 Principal Directors' Duties

A series of statutory duties apply to directors of companies incorporated in the UK. These continue to apply to such companies in a bid scenario. For example, under the Companies Act 2006, it is the primary duty of directors to act in the way which they consider, in good faith, would be most likely to promote the success of the company for the benefit of its shareholders as a whole.

In fulfilling this duty, they must have regard to six factors, including the likely consequences of any decisions in the long term and the interests of employees. Note that the duty itself is owed only to the company. These matters are non-exhaustive. For example, it may be appropriate on the facts to have regard to short-term as well as long-term consequences.

There is case law suggesting that directors owe certain particular duties to shareholders in a takeover situation. Examples include a positive duty to make full disclosure of all relevant information, express honest opinions on the merits of the offer and generally not to mislead shareholders. Such duties correspond to a large extent with the directors' responsibilities regarding information under the Code.

The Code does not prescribe the factors which the target board may or shall consider in deciding whether to recommend an offer and giving its opinion on the offer (these factors are invariably dictated by the directors' statutory duties). There is no limit to the factors which the board can take into account and it does not need to consider the offer price as the only or determining factor, although in practice this is often paramount.

There are also various duties and obligations imposed on the directors of the bidder and target under the Code and otherwise, as described in other sections of this guide. These include any requirement to announce, take independent advice, treat shareholders equally and disclose and take responsibility for information published in connection with a bid.

8.2 Special or Ad Hoc Committees

It is common for the bidder and target boards to delegate day-to-day responsibilities relating to the bid to a committee. However, the Code broadly provides for all directors (whether members of the committee or not) to remain personally responsible for complying with the Code despite any delegation.

Committees are also frequently used where there is a conflict of interest for some directors. This allows the board to establish an independent body to conduct and consider the bid separately from the interested directors; for example, if the deal is a management buyout.

8.3 Business Judgement Rule

English courts will typically only be involved in takeovers effected by way of a scheme that involves a court procedure and requires the court's sanction, and do not involve themselves in reviewing the judgement of directors relating to a takeover or the fairness of its terms. Given that schemes tend to relate only to recommended offers, the directors of the target are usually supportive of the offer and the courts are likely to take this into account.

As discussed above, in Re Expro International Group Plc, it was noted that it is not appropriate for the court procedure involved in a scheme to allow an undesirable level of uncertainty which the provisions of the Code have successfully reduced or eliminated in the case of ordinary offers. In this particular instance, at the court hearing seeking the sanction of a scheme of arrangement, certain shareholders of the company appeared and sought an adjournment of the company's application for the sanction of the scheme for 14 days in order for an American-based consortium to make a further bid for the company. The court did not permit the adjournment as doing so would perpetuate the uncertainty to the potential disadvantage of the shareholders.

There is a similar concept under English law that the court will not interfere with the directors' decision unless no reasonable board could have come to that decision. The directors' judgement is not often challenged in takeovers, not least because takeovers are not effected by the target entering into an agreement previously approved by the board but are more typically an arrangement entered into with the target's shareholders.

8.4 Independent Outside Advice

The Code requires the target board to seek competent independent advice (typically from an investment bank or accountancy firm) in relation to the merits of an offer. The substance of the advice must be made known to shareholders in the offer document (in a recommended bid) and the defence documents (in a hostile bid).

The main duty of the independent adviser to the target board is to advise it on whether the financial terms of the offer are fair and reasonable. More generally, the parties to a takeover offer will in any event have financial and legal advisers who will advise them on their duties under the Code and in relation to the steps and documents required to implement the takeover. Financial advisers have particular duties under the Code (for example, to inform clients of the importance of security and secrecy before announcement, and to ensure the availability of sufficient funding to satisfy in full the cash component of any offer consideration).

8.5 Conflicts of Interest

Target directors connected to the bidder are not independent and cannot participate in the target board's recommendation.

The Panel's consent is needed under Rule 16 of the Code before any special deals with favourable conditions can be entered into with some shareholders, which are not extended to all shareholders. Typically in the case of management buyouts, approval of any equity package to management would be required by a vote of independent target shareholders.

As noted above, under Rule 3 of the Code, the target board must obtain competent independent financial advice on any offer. The Rule 3 adviser must be independent of the bidder and the offer. A person who is in the same group as the bidder's financial or other professional adviser would not be regarded as an appropriate person to give independent advice, nor would someone who has a significant interest in, or financial connection with, the bidder or target.

There have been notable cases regarding conflicts of interest in relation to advisers. In 2004, Marks & Spencer was granted an injunction to restrain its lawyers from acting for a consortium led by Philip Green, which was undertaking an attempted hostile takeover of the company, on the basis that they were acting for the company in other non-contentious transactions and so there was a conflict of interest.

In addition to complying with the Code requirements relating to independence, target directors will also be mindful of the statutory duty of directors to avoid conflicts of interest under the Companies Act 2006.

9. Defensive Measures

9.1 Hostile Tender Offers
Hostile tender offers are uncommon in the UK, with usually only a few each year. The most well-publicised examples in recent times were Pfizer Inc's possible offer for AstraZeneca in 2014 (which did not go ahead), Kraft's takeover of Cadbury in 2010 and Essar Global Fund Limited's offer for the minority shares it did not own in Essar Energy plc in 2014. However, many hostile approaches are ultimately recommended, as with the Kraft/Cadbury takeover. Examples of hostile takeovers in 2016 include the proposed offer by McCormick & Co Inc for the entire share capital of Premier Foods plc and the proposed offer by AFH Financial Group PLC for the entire issued share capital of Lighthouse Group plc (both of which did not go ahead).

Since 19 September 2011, target boards have had greater protection from hostile offers. For example, the PUSU regime requires a prospective bidder to make a formal offer within 28 days of expressing its interest, or walk away. This has deterred some hostile offers, because the unwelcome bidder has limited time to canvass target shareholders, conduct due diligence and prepare funding arrangements.

9.2 Directors' Use of Defensive Measures
Target directors may use limited defensive measures following a hostile bid, provided that they do not conflict with the general law, including their statutory duties, or the Code.

However, the Code requires that during the course of an offer, or if the target board has reason to believe that a bona fide offer might be imminent, shareholder consent is obtained before taking any action which may result in any offer or possible offer being frustrated or in shareholders being denied the opportunity to decide on its merits. This in practice prohibits the target board from taking certain defensive measures (including any such measures which are commonly used in the US). In particular, they cannot authorise a substantial acquisition or disposal during an offer period if the assets are of a material amount. The use of poison pill measures to render a target bid-proof or unattractive to potential bidders is also prohibited. They are unable to arrange for the target to declare and pay an interim dividend during an offer period, other than in the normal course.

There are various steps that a company which considers itself at risk of a takeover may take. Often a defence manual will be prepared to record these. Possible preparatory steps include monitoring the company's share register for unexpected changes, maintaining contact with major institutional investors to garner their support, establishing guidelines for dealing with analysts, preparing responses to brokers' circulars and providing appropriate information packs for journalists.

9.3 Common Defensive Measures
The target board may seek an alternative third party (a "white knight") to make an alternative bid but must bear in mind its statutory duties. The Panel will usually allow a target to enter into an inducement fee arrangement with one or more white knights up to an aggregate value not exceeding 1% of the target's value.

The directors may seek to make the target less attractive to the bidder by undertaking a substantial acquisition or disposal, provided the assets are not of a material amount, or demerging parts of the business integral to the bidder's offer. Providing information to a regulatory authority which undermines a bidder's position is a further option. Another, in the case of a securities exchange bid, is to question the bidder's status and financial position.

9.4 Directors' Duties
As mentioned in **8.1 Principal Directors' Duties**, directors are under a statutory duty to promote the success of the company for its members. The factors which they should take into account include the long-term consequences of a decision. This is usually interpreted to allow directors to promote a long-term increase in value of the company. When enacting defensive measures, directors must consider all aspects of the offer, such as the offer price, the effect of implementing the bid on employees and employment conditions, and any short-term gains as against long-term disadvantages.

Directors must also exercise their powers under the company's constitution in accordance with the purposes for which they were conferred. This prevents them from issuing new shares to frustrate a hostile bid.

9.5 Directors' Ability to "Just Say No"
Directors must be mindful of their legal duties; they cannot simply say 'not for sale'. One of the most common strategies for fighting off a hostile bid is to urge shareholders to reject the offer. The directors may seek to do this by disclosing new information in the form of profit forecasts, asset valuations, quantified financial benefits statements quantifying the anticipated benefits from activities proposed if the bid fails and preliminary and interim results, to argue that the bidder undervalues the target. It will be important to follow closely the provisions of the Code which apply to such measures. An alternative approach is to implement arrangements that will return funds to shareholders should the offer be unsuccessful, subject to consulting the Panel and obtaining shareholder approval as required under the Code. The Code sets out restrictions on other defensive activity, however.

10. Litigation

10.1 Frequency of Litigation

Public takeovers are monitored by the Panel. On a contractual offer, the courts will not typically be involved in the process and will only intervene in exceptional circumstances. During the takeover of Datafin in 1986, the Court of Appeal decided that, whilst decisions of the Panel are subject to judicial review, the courts will be reluctant to entertain litigation during offers because it creates uncertainty and so is against the interests of shareholders.

In a limited number of instances, minority shareholders have raised objections to schemes at the court sanction hearing. These typically challenged the scheme on the basis that the procedural requirements were not followed; for example, correct notice of meeting was not given or the explanatory statement was not properly despatched, or a class of shareholders was not fairly represented, or approval of the scheme was not reasonable.

The court may order certain modifications to the scheme or may refuse to sanction it altogether. Alternatively, the court may reject the challenge and sanction the scheme. For example, the scheme to implement the takeover of TDG plc by LIT plc in 2008 was challenged by a minority shareholder at the court approval stage on the grounds that the class of shareholders subject to the scheme had not been fairly represented by those attending the meeting. The court rejected the challenge, since there was no proof that the statutory majority was not acting bona fide or was coercing the minority to protect adverse interests. In the case of Fitness First Finance, the High Court sanctioned a scheme of arrangement with reference to the principles set out in Re TDG PLC that the court, in sanctioning a scheme of arrangement, must be satisfied that *inter alia* : (i) the provisions of the statute have been complied with; (ii) the class of shareholders at the court meeting is fairly represented by those attending; (iii) the arrangement is one that an intelligent and honest man, a member of the class concerned, and acting in his own interests, might reasonably approve; and (iv) there is no blot on the scheme.

10.2 Stage of Deal

As outlined in **10.1 Frequency of Litigation**, litigation remains rare in the context of a UK takeover.

11. Activism

11.1 Shareholder Activism

Shareholder activism has become an increasing trend in the UK, but it remains rare and is not a material factor in merger and acquisition transactions, in part because the Code regulates "board control-seeking proposals". More than 20 British companies had been publicly subjected to activist demands in 2015.

That said, some of the more high-profile instances of shareholder activism include the appointment of Edward Bramson to the board of Electra Private Equity following a failed attempt by Sherborne Investors to do so in 2014. Similarly, Elliott Investors (which has been involved in multiple activist campaigns in the United Kingdom since 2010) and ValueAct Capital have both requisitioned general meetings to propose director appointments to the boards of Alliance Trust and Rolls-Royce respectively. Separately, in 2013, Sherborne had acquired shares in 3i and reportedly wanted to push for increased cash returns to shareholders, although ultimately it sold shares at a profit. A possible activist tactic is to pressurise bidders to implement share buybacks and dividends.

Shareholder activists use various techniques to block resolutions from being passed, including contacting other shareholders or making public announcements to voice concerns and persuade other shareholders of their viewpoint, or buying shares to build up a stake, or mustering enough support from other shareholders. An alternative approach is to requisition a general meeting to consider resolutions, most commonly, over board changes. In either case, activists will use statutory rights to requisition the meeting and propose resolutions to the meeting.

In practice, perhaps the greatest shareholder influence in the UK is exercised by major institutional investors who command a significant voice because of their shareholdings and reputation in the market. Such influence is generally badged as 'stewardship' rather than 'activism' and is important in the context of investor relations, board relationships and support for or defence from takeover offers.

11.2 Aims of Activists

The base case for UK PLCs is that a special resolution (75%) is required to direct board action – so a lot of activism is focused on forcing board change if desired corporate is not taken (which can be achieved by ordinary (50%) majority). Nevertheless, various instances of 'deal activism' (that is, shareholders seeking to interfere with a corporate transaction) have been reported recently, both in support of acquisitions and disposals. Often this is provoked through 'stewardship' initiatives rather than more aggressive activist tactics. For example, Cevian Capital was understood to have demanded the sale of G4S' cash solutions unit in 2013. Charterhouse Capital Partners offered to buy the cash solutions unit of G4S for USD $2.5 billion but this was ultimately rejected by the board.

11.3 Interference with Completion

For the reasons explained in section **10 Litigation**, the courts rarely interfere in M&A processes. Activists do, however, seek to influence completion of announced transactions. For example, when G4S announced its intention to acquire cleaning group ISS for GBP5.2 billion, Parvus Asset Management took ownership of a stake in G4S after swapping out contracts for difference, making it one of the largest shareholders in G4S. Parvus publicly expressed its opposition to the deal by stating that the acquisition made little sense strategically, operationally or financially. Shareholders ultimately voted against the acquisition. More recently, in 2015 Paulson & Co and Standard Life (both minority shareholders each owning approximately 7% of Premier Foods shares) publicly attacked the board of Premier Foods for: (a) a failure by it to engage in discussions regarding a takeover approach from McCormick, and (b) electing to collaborate with Nissin Foods instead.

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