

May 17, 2022

Changes to U.K. Takeover Code

Amendments of Particular Significance for Bidders

SUMMARY

On May 5, 2022, the U.K.'s Panel on Takeovers and Mergers (the "**Panel**") published the results of a consultation that started in December 2021 to review the City Code on Takeovers and Mergers (the "**Code**"), together with proposed amendments to the Code. The amendments cover a broad range of topics, a number of which are of particular significance for prospective bidders.

In summary, the amendments:

- require bidders to disclose in possible offer announcements whether they are obliged under the Code to offer a minimum level, or particular form, of consideration;
- prevent bidders who have made a mandatory offer from acquiring further target shares in the 14-day period before shareholders must decide whether or not to accept the offer;
- clarify that the 12-month look-back period used for determining the price of a mandatory offer runs from the date on which the offer should have been announced; and
- reform the circumstances in which bidders can be required to make a mandatory offer by virtue of the "chain principle", by removing the "significant purpose test" and reducing the threshold under the "significant interest test" from 50% to 30%.

The amendments to the Code will take effect from June 13, 2022. Any ongoing transactions will be subject to the amended provisions, except where to do so would give the amendments retroactive effect.

THE KEY CHANGES

The key changes are summarised below.

A. DISCLOSURE OF OBLIGATION TO OFFER A MINIMUM LEVEL, OR PARTICULAR FORM, OF CONSIDERATION

Acquisitions by bidders, or their concert parties, of interests in target shares can, in certain circumstances, require any offer made to target shareholders to include a minimum level of consideration, or a particular form of consideration. In particular, any such acquisitions may:

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- establish a floor price for the offer, if any interests in target shares are acquired during a defined period (normally the three months before an offer period — i.e. before there has been a possible offer announcement or a firm offer announcement — and during an offer period); or
- require any transaction to be 100% in cash (or with a 100% cash alternative), if interests in shares carrying 10% or more of the voting rights in the target are acquired for cash within 12 months prior to the offer period or at any time during the offer period.

Any announcement of a firm intention to make an offer must include the price at which the offer will be made as well as the form of consideration. As a result, under the current Code, bidders must ascertain whether they are required to comply with any obligation to offer a minimum level, or particular form, of consideration before announcing a firm intention to make an offer.

Under the revised Code, any possible offer announcement made by a potential bidder must include details of any minimum level, or particular form, of consideration that would need to be offered as a result of the bidder's own acquisition of interests in target shares. No negative statement is required if the bidder is not subject to such a requirement.

Likewise, a possible offer announcement made by the target with the potential bidder's agreement and approval must include such a statement (if applicable). If the target unilaterally announces a possible offer, any potential bidder identified in the announcement will need to make its own announcement containing such a statement as soon as practicable thereafter.

The Panel recognises that it may not always be practical for a potential bidder, before a possible offer announcement is made, to have made enquiries of all of its concert parties so as to ascertain whether their dealings trigger an obligation to offer a minimum level, or particular form, of consideration. As a result, a bidder is required to announce any minimum level, or particular form, of consideration required to be offered as a result of its concert parties' acquisition of interests in target shares as soon as reasonably practicable after the possible offer announcement is made, and in any event by no later than 12 noon (London time) on the tenth business day following that announcement.

The practical effect of these changes is that a potential bidder, in conjunction with its advisers, will need to have ascertained whether it is subject to an obligation to offer a minimum level, or particular form, of consideration at an earlier stage of the process than under the current Code. This is because a bidder must be prepared to make a possible offer announcement from the time that it first "actively considers" acquiring the target — i.e. where its assessment of the target increases in intensity to a level where it is being given more serious consideration than a routine assessment of a potential acquisition target's performance. From such time, the Panel can require a bidder (or the target once it has been approached by the bidder) to make an announcement if there is a leak or a material or abrupt movement in the target's share price.

Whilst a bidder can typically assess very quickly whether it (or any of its subsidiaries) has acquired interests in target shares which could trigger an obligation for any offer to include a minimum level, or particular form, of consideration, it often takes more time for a bidder to ascertain the past dealings of

its concert parties (as the Panel recognises), in particular given the need to maintain secrecy prior to an announcement. This is particularly the case where the concert party is wide, for instance if the bidder is a private equity firm or part of a financial services group. To comply with the new requirements, upon entering active consideration bidders will need to implement processes so that they can have confidence in ascertaining their concert parties' past dealings within ten business days of any possible offer announcement (if not before).

The revised Code will also require all bidders or potential bidders whose existence has been referred to in any announcement (whether publicly identified or not) or who are participating in a formal sale process to make an immediate announcement if they, or their concert parties, acquire interests in target shares during an offer period which trigger the requirement for any offer to include a minimum level, or particular form, of consideration.

It remains to be seen how the Panel intends these new rules to interact with the existing obligations of pre-announcement secrecy set out in the Code, particularly the requirement not to approach more than six persons outside the parties to the offer (and their immediate advisers) without the Panel's consent. The Panel should be consulted if, in order to facilitate compliance with the new rules, it is proposed that a significant number of concert parties will be contacted pre-announcement.

B. RESTRICTIONS ON ACQUISITIONS OF INTERESTS IN SHARES BY A MANDATORY BIDDER AT THE END OF THE OFFER TIMETABLE

The revised Code will ban mandatory bidders, and their concert parties, from acquiring interests in target shares during the 14 days prior to the deadline for the satisfaction of all conditions (or during the 14 days prior to any earlier date on which the bidder intends to lapse its offer by issuing an acceptance condition invocation notice).

Under the current Code, a mandatory bidder can acquire target shares at or below the offer price during this 14-day period. This has meant that target shareholders may have to decide whether or not to accept a mandatory offer without knowing the proportion of shares the mandatory bidder will hold if the offer fails. The Panel views this as important information that target shareholders should know with certainty when deciding whether or not to accept a mandatory offer.

C. THE "LOOK-BACK PERIOD" FOR DETERMINING THE PRICE OF A MANDATORY OFFER

A mandatory offer must be made at no less than the highest price paid by the mandatory bidder, or its concert parties, for interests in target shares during the 12 months prior to its announcement of a mandatory offer. A mandatory offer needs to be announced immediately following the acquisition of interests in target shares that gives rise to the obligation to make the mandatory offer.

The revised Code clarifies that, if the mandatory offeror does not make such an announcement immediately, the 12-month look-back period is nevertheless set by reference to when such an announcement ought to have been made, rather than when it actually was made. This codifies the

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Panel's current practice and serves to prevent a mandatory offeror from manipulating the price of its offer by delaying the announcement of the offer.

D. REFORM OF THE CHAIN PRINCIPLE

A mandatory offer can be required if a person (or a group of persons acting in concert) ("A") acquires 50% or more of the voting rights of a company ("B") where B holds 30% or more of the voting rights in a second company ("C"). C must be a company to which the Code applies, but B need not be. In such circumstances, the "chain principle" may require A to make a mandatory offer for the shares in C that are not already held by B (as occurred in 2018 when the Panel ruled that Disney, which had agreed to acquire 21st Century Fox, which held a 39% stake in Sky, was required to make an offer for Sky under the chain principle). The chain principle is designed to protect the other shareholders in C, who may be prejudiced if ultimate control of C passes to A without them being given an opportunity to exit C at the same implied premium per C share as the shareholders in B.

Under the current Code, the chain principle will normally apply if:

- the interests in shares which B has in C is significant in relation to B. In assessing this, the Panel will consider a number of factors, including the assets, profits and market values of the respective companies (the "significant interest test"). Relative values of 50% or more will normally be regarded as significant; or
- securing control of C might reasonably be considered to be a significant purpose of A's acquisition of control of B (the "significant purpose test").

The revised Code will delete the significant purpose test, on the basis that the Panel considers that it provides a low threshold that is likely to be satisfied in every case where the significant interest test is also satisfied.

The significant interest test will be retained, although the relative values that will normally be regarded as significant will be reduced from 50% to 30%. The Panel considers that this strikes an appropriate balance between capturing transactions where C is likely to be significant to A whilst at the same time not inappropriately impacting the value of B.

The Panel will retain flexibility to require chain principle offers even when the significant interest test is not satisfied, but the Code Committee expects that this flexibility will be used only in exceptional circumstances (e.g. where it is apparent that an acquisition has been deliberately structured so as to avoid being caught by the proposed 30% threshold).

E. OTHER CHANGES

The revised Code amends some of the technical rules relating to the situation where a party is restricted from making an offer (either because it has made an offer which has lapsed or because it has made a "no intention to bid" statement), in particular the rules relating to:

- the circumstances in which a bidder that made a "no increase statement" or an "acceleration statement" in relation to an offer which subsequently lapsed can proceed to make a new offer

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(where, under the new rules, a bidder who made such a statement and wishes to make an improved offer will usually be restricted from making such improved offer until the later of three months from the date on which the previous offer was withdrawn or lapsed and the end of the offer period for the target);

- the period of time for which a potential bidder who has made a “no intention to bid” statement should be bound by any prior statement as to the terms on which a possible offer might be made (where, under the new rules, the potential bidder will be bound by this statement until the later of three months from the date on which the “no intention to bid” statement was made and the end of the offer period for the target); and
- the circumstances in which a bidder whose offer has lapsed can proceed to make a new offer if a third party announces a firm intention to make an offer for the target (where it has been clarified that a “third party” may include a potential bidder which had been publicly identified prior to the date on which the previous offer was withdrawn or lapsed).

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