

Some significant changes to the Takeover Code - the end of the road for inducement fees?

The Code Committee of the Takeover Panel (“**Panel**”) today published the much awaited response to its public consultation paper of 1 June 2010. The paper itself was published in the wake of the controversy surrounding the Kraft takeover of Cadbury earlier this year. The Panel is unhappy that, in recent times, bidders have been able to gain a tactical advantage over target companies to the detriment of those target companies and their shareholders. The Panel is now seeking to redress the balance in favour of the target. This involves a number of interesting and potentially controversial proposals, including a ban on deal protection measures and inducement fees.

Where appropriate, the Panel intends to implement the proposals by amending the City Code on Takeovers and Mergers (“**Code**”). Any amendments will be made after public consultation by the Panel setting out the proposed amendments in full in accordance with the Panel’s usual procedures.

Proposed changes to the Code

- **The Code will ban deal protection measures and inducement fees except in limited cases.** The Panel feels these measures are often presented to target company boards as standard “packages” putting them under huge pressure to accept. They can also deter competing offers. So, the Code will contain a general prohibition on undertakings given to a bidder by a target to take action to implement a Code transaction or to refrain from action which might help a competing Code transaction. There will also be a blanket ban on inducement fee arrangements. Certain specific undertakings will be allowed relating to confidentiality, non-solicitation of employees/customers and the provision of information required to satisfy the conditions of the offer or obtain regulatory approvals. The ban will not apply where the target has been put up for sale by way of public auction and will not prevent the grant of undertakings required as a matter of implementing takeovers by way of a scheme of arrangement.
- **Targets will benefit from more protection in “virtual bids”** i.e. where a potential bidder announces its intention to make an offer but does not commit itself to do so. Potential bidders will have to be named in the announcement which starts an offer period, regardless of which party publishes the announcement. Any publicly named potential bidder will have four weeks to announce its intention to proceed or not proceed with the offer. The Panel believes this will give target companies more timing certainty and reduce the period during which they are effectively under “siege” from unsolicited or unwelcome potential bidders. These rules will not apply where the target has been put up for sale by way of public auction.
- **The Panel has decided not to introduce a formal “put up or shut up” regime in a private context** as the target is under less pressure in that case but the Panel may agree to this on an exceptional basis.
- **The Code will clarify that target boards are not limited in the factors which they can take into account in giving an opinion on an offer** and are not bound to consider the offer price as a determining factor.
- **The Code will require better quality disclosure of the bidder’s intentions regarding the target and its employees.** Bidders will still, as now, have to disclose details of plans for the target’s employees, locations of business and fixed assets but statements on these issues will be expected to hold true for at least one year after the offer becomes wholly unconditional. Also, bidders will have to make a negative statement if there are no such plans. This recognises that the ability of the target directors to comply with their own obligations, and to provide meaningful information to shareholders and employees, depends on the accuracy and adequacy of the information published by the bidder.

- **Various provisions will be introduced to encourage and augment communication between the target board and employees/employee representatives** including an obligation on the target to pay the costs incurred by employee representatives in verifying information given to them by the target for the purposes of their opinion.
- **There will be more prescriptive rules on the disclosure of advisory fees** including a requirement to disclose the minimum and maximum amounts payable under advisory success fees by category of adviser (e.g. financial advisers, lawyers etc). Fees in respect of financing will have to be disclosed separately from advisory fees.
- **The Code will require further disclosure by bidders in relation to the financing of the offer** including the implications that the offer financing might have on the bidder, target and their respective businesses going forward. Bidders will have to provide detailed financial information about themselves for all offers, not just securities exchange offers. Also, where the offer is material, the offer documents must contain a pro forma balance sheet of the combined group, details of the ratings given to the bidder by ratings agencies (and changes in those ratings resulting from the bid) and greater detail about the debt facilities or other instruments used to finance the offer.
- **Disenfranchising shares acquired during the offer period**, i.e. withholding voting rights from shares acquired during an offer period. The Panel is not proposing to pursue this. Many respondents to the 1 June consultation paper shared the concern that this could compromise the principle of “one share, one vote”, and could run contrary to the general principle of equivalent treatment for all shareholders. Again, the Panel notes that if qualifying periods (or weighted voting rights) were to be introduced through changes in company law, it would be logically consistent for the Code to be amended in the same way.
- **Providing protection to bidder shareholders.** The Panel is not proposing any changes to the Code on this point. However, as referred to earlier, the Panel does suggest further disclosures should be made in offer documents in relation to the financial position of the bidder and its group and the financing of the offer, and the bidder’s future intentions relating to the target and its employees.

The 1 June consultation paper discussed a number of other suggestions for amendments to the Code, including shortening the offer timetable and separate advice for target shareholders. The Panel has decided not to implement these proposals at the moment.

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Proposals which are not being adopted

Other proposals which were discussed in the 1 June consultation paper which are not being adopted include:

- **Raising the acceptance condition threshold above “50% plus one”.** This threshold is founded upon and inextricably linked with the threshold for passing an ordinary resolution under UK company law. The Panel is not proposing to raise the acceptance condition threshold but says it would be logical to do so if company law is amended to raise the ordinary resolution threshold.

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