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TAKEOVERS PANEL

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Cost disputes now to be determined by the Panel

Until a recent amendment to the Takeovers Act 1993, rule 49 of the Code provided that target companies, and their directors, were entitled to recover from an offeror any expenses properly incurred in relation to an offer or takeover notice. Disputes about rule 49 reimbursements were adjudicated by the District or High Court, although were often settled out of court.

Rule 49 has now been replaced by new sections 47-53 of the Takeovers Act. Target companies, and their directors, are still entitled to recover from an offeror any expenses properly incurred in relation to an offer or takeover notice, but the new provisions transfer to the Panel the role of primary adjudicator of reimbursement disputes. The Panel has published the new *Guidance Note on the Process for Costs Reimbursements under the Takeovers Act* on the matter.

Call scripts, shareholder presentations, slides and other information published or sent to offerees – a reminder to the market

Rule 47(4) provides that an offeror or target company or person acting on behalf of any of them who, in relation to an offer or a takeover notice, publishes or sends to any offeree any statement or information that is not required to be published or sent under the Code must, at the same time that the statement or information is published or sent, also send a copy of it to the Panel. Rule 19A(2) is in similar terms in respect of documents relating to shareholder meetings held under rule 7(c) or (d).

The Panel is aware that there may be some confusion in the market about the breadth of rule 47(4) and rule 19A(2) of the Code. In recent takeover transactions, parties were unclear whether call scripts, shareholder presentations and slides, and other similar documents or information must be sent to the Panel.

Consistent with the common law, to 'publish' information to offerees is construed widely by the Panel, and includes information conveyed to shareholders at investor meetings or by telephone. This means that slides or presentation notes for meetings with offerees, call scripts and associated 'question and answer' scripts that are used by, or on behalf of, offerors or target companies are all required to be provided to the Panel.

Date of target company statement

Rule 46 of the Code requires a target company to send a target company statement ("TCS"), but the Code does not specify how to determine the TCS. However, clauses 5 and 6 of Schedule 1 to the Code require that the TCS includes or is accompanied by the date for information about the ownership of equity securities of the target company and trading in target company equity securities over time periods defined by reference to the date of the TCS, so the date of the TCS can have a material effect on the disclosures made in the TCS.

While there are no explicit rules in the Code regarding the date of the TCS, the target company is subject, as always, to rule 64's prohibition on misleading conduct. The greater the discrepancy between the date of the TCS and the date on which the TCS is sent to shareholders and the offeror, the more likely that the information in the TCS will be inaccurate and possibly misleading to shareholders, and consequently be in breach of rule 64.

Furthermore, rule 46 requires the target company to send the TCS either:

(a) to the offeror within 14 days after it receives the takeover notice (or any longer period as the offeror may allow) (rule 46(a)(i)); or

(b) to the offerees within 14 days after it receives the despatch notice (rule 46(a)(ii)).

In non-hostile takeovers, target companies can send the TCS in accordance with rule 46(a)(i) in order to allow the TCS to be sent to shareholders concurrently with the offer document. In that scenario, it would be common for the TCS to be dated on or about the date of the offer document.

A far more common scenario, and certainly when the takeover is hostile, is that the TCS is prepared in response to the offer document and so is sent in accordance with rule 46(a)(ii). In that scenario, it would be counterintuitive and arguably misleading for the TCS to be dated prior to the date on which the offer document was sent.

While the dating of a TCS will depend on the circumstances of the takeover to which it relates, target companies should be mindful of their obligations under the Code. Legal advisers are reminded that the Panel executive is available to discuss Code matters on a confidential basis. If there is any doubt as to whether dating a TCS in a particular way may mislead shareholders, the Panel executive is available to discuss the issues.

Recent application and interpretation of rules 42A and 42B

During a recent full takeover offer, the Panel was asked to consider whether a conditional right to be issued shares in the future was an 'equity security' for the purposes of the Code. It was an important question in the context of the takeover, because if the conditional right was an equity security, the offeror would have to make an offer for the conditional right, and would need an independent adviser to prepare a report under rule 22 of the Code regarding the fairness of the consideration as between the classes of securities.

The conditional right to be issued shares arose out of the sale of a business to the target company. The sellers were to be issued with shares in the target company, by way of additional consideration, if certain performance targets were met following the sale (i.e., an earn-out arrangement).

It was submitted to the Panel by the acquirer that the Code does not contemplate offers being made in respect of such a conditional right, because compliance with rules 42A and 42B of the Code would be impossible.

Rule 42A requires that the class notice sent to the offeror by the target company contains sufficient information about each class of equity security to enable the offeror to formulate an offer, and rule 42A(4) states that "sufficient information" includes the terms of issue of each class of security and the number of those securities on issue in each class. It was submitted that this was problematic in the circumstances because there was no equity security (such as an option) with terms that could be disclosed in the normal sense and because the number of shares to be allotted depended on a future event and could not be included when the class notice was sent.

Rule 42B requires that the target company sends to the offeror a copy of its financial products register relating to the financial products to which the offer relates. While a right to be issued shares may be listed on a financial products register (as is often the case for convertible rights), it may not be listed at all (as was the case here). If it is not listed, it was submitted that the target company will be unable to comply with rule 42B because it cannot provide a copy of a financial products register that does not exist.

"Equity security" is defined in rule 3 of the Code as:

equity security –

(a) means any interest in or right to (whether carrying voting rights or not)—

(i) a share in a company or other body corporate; or

(ii) the share capital of a company or other body corporate; and

(b) *includes an option or right to acquire any such interest or right unless that option or right is exercisable only with the agreement of the issuer; but*

(c) *does not include redeemable financial products that are redeemable only for cash.*

Sub-clause (b) of the definition of equity security clearly includes a right to acquire a share of a company in the future. Irrespective of whether the right is conditional, one party has a right to acquire shares and the other party has a corresponding obligation to issue shares.

On that basis, the relevant "equity security" comprised the provisions in the sale agreement giving rise to the potential future issue of shares in the target company.

Accordingly, applying a purposive interpretation, compliance was achieved by providing the offeror with a description of the terms of the earn-out arrangement, including the circumstances in which the sellers would be entitled to receive shares and the number of shares to be issued or the way in which the number of shares to be issued would be determined.

The purpose of rule 42B is to ensure that the offeror is given information that enables it to send its offer to the holders of each class of equity security. It would be inconsistent with the purpose of that rule to treat the lack of a financial products register relating to the conditional right as being determinative of whether that conditional right is in fact an equity security.

Compliance with rule 42B can be achieved by creating a financial products register of equity securities specifically for the purposes of rule 42B.

This recent takeover offer demonstrates the need for target companies to fully disclose their equity securities, including conditional rights to issue equity securities.

Guidance Notes have been updated

In line with other regulators in the financial markets, the Panel encourages clear, concise and effective drafting. The Guidance Notes for *Offer Documents*, *Independent Advisers* and *Target Company Statements* have been updated to reflect the Panel's expectation of clear, concise and effective disclosure in Code documentation.

Class exemption notice has been updated

Finally, two new clauses have been inserted into the *Takeovers Code (Class Exemptions) Notice (No 2) 2001.*

New clause 25D grants an exemption from rule 44(1)(d)(ii) of the Code, which requires a takeover offer to contain any additional information that was contained in the takeover notice. The exemption applies where any of the additional information in the takeover notice is found to be erroneous or outdated.

New clause 25E grants an exemption from rule 44(1)(b), which requires an offer to be on the same terms and conditions as those contained in the draft offer document accompanying the takeover notice. The exemption applies where a variation to the terms or conditions contained in the draft offer is approved by the Panel and is to correct an obvious technical error that is minor in nature.

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