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# Corporate M&A

**UK: Law & Practice**

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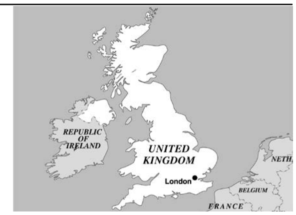
# UK

## Law and Practice

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## Contents

# 1. Trends

## 1.1 M&A Market

The UK M&A market can be categorised in three ways:

- domestic M&A – UK companies acquiring other UK based companies;
- inward M&A – mergers, acquisitions and disposals of UK companies by overseas companies; and
- outward M&A – mergers, acquisitions and disposals of overseas companies by UK based companies

Focussing on mergers and acquisitions in respect of companies valued at GBP1 million or above in 2019 Domestic M&A fell on average GBP4.9 billion per quarter whilst Outward and Inward M&A also dropped by GBP0.35 billion and GBP7.57 billion respectively when compared to quarter averages in 2018. Data for the final quarter of 2019 is not yet available.

In terms of number of deals, again each category has shown average decreases between 2018 and 2019.

The public M&A market has actually increased in 2019 when considering overall bid activity. Hostile bid activity (bids which have not been recommended by the target's board of directors) has increased, as well as competitive bids (where there is more than one bidder in respect of a target company).

## 1.2 Key Trends

The key trends of 2019 were not dissimilar to the preceding year; convergence continued to be a catalyst for deals especially in the telecom industry. Activism has increasingly become an acceptable practice with the focus shifting to corporate governance.

Disruptive and innovative technologies remain at the heart of M&A activity with reports companies spent USD217 billion making acquisitions in this sector in 2019 which is an increase of 28% from 2018.

Uncertainties stemming from global factors such as trade wars or increased regulation did not impact M&A transactions as significantly as anticipated, neither did Brexit in terms of domestic activity.

## 1.3 Key Industries

The technology sector has continued to be an active industry in 2019 accounting for 15% of public offers announced. The hospitality industry given the challenges it faces saw an increase in consolidations both within hotels group and the public houses.

Notwithstanding pharmaceuticals, biotech and the healthcare sector was relatively active in 2018 this trend did not continue in 2019 which saw a decrease in activity in these industries.

Based on available data overall the first half of 2019 evidenced most activity in the financial services, info communications and manufacturing sectors. Technology, media and telecom industry also remained active and this is likely to continue given the prevalence of online film and television viewers.

# 2. Overview of Regulatory Field

## 2.1 Acquiring a Company

**Private**

The acquisition of a private company is dependent on identifying a willing seller. Once you have a willing seller you can acquire a private company in the UK either by way of a share purchase or an asset purchase. Whilst either way will achieve broadly the same commercial objective there are important legal and tax differences between the two structures.

***Asset purchase***

This is the purchase of specific assets (and sometimes) liabilities which comprise the business. The parties will negotiate and agree which assets are being acquired and those which will remain in the selling company. In this way the buyer does not acquire the limited company itself, but instead it buys certain elements which make up the business (eg, business records, equipment, stock, goodwill, the business contracts, intellectual property). This has the advantage for the buyer in that it can be selective with what is included within the purchase and the buyer can exclude any assets/liabilities which it considers problematic. Various consents and approvals may need to be sought in order to transfer the agreed assets. With an asset sale the funds will be paid directly to the limited company with limited involvement from the company's shareholders as opposed to a share sale which involves direct payment to the shareholders.

The transfer of assets involves tax considerations such as VAT, transfers of going concern, Stamp Duty Land Tax, deductions of acquisitions cost and corporation tax. Asset purchases are also likely to fall under the scope of Transfer of Undertakings (Protection of Employment) Regulations 2006 (SI 2006/246) (TUPE), which provides for certain employee protections as part of the transfer of assets.

An asset purchase is usually effected by entering into a business purchase agreement which will cover:

- provisions identifying which assets are included and excluded from the sale;

- limited warranties;
- apportionment of liabilities and obligations between the buyer and seller in relation to the assets being transferred; and
- restrictive covenants.

Tangible assets are delivered to the buyer and intangible assets are formally assigned in a deed.

*Share purchase*

This is where the shares in the limited company are purchased such that ownership of the assets and business will remain within the limited company but the overall ownership of that company is transferred. As the trading entity does not change business continuity is preserved. The transfer is "warts and all" meaning that the buyer as the new shareholder of the company will take over all assets and liabilities. This presents a significant risk to any buyer making the due diligence process all the more important.

A share purchase is effected by entering into a share purchase agreement with the following provisions:

- warranties;
- indemnities;
- tax covenant; and
- restrictive covenants.

On completion of the share purchase agreement a stock transfer form will be executed by the seller and new share certificates issued to the buyer.

**Public**

Public companies are acquired through the purchase of all or a substantial part of the shareholding. This can happen in two ways, namely; recommended (ie, with approval of the target board) or hostile where the management team has publicly advised the shareholders to reject the offer to prevent the takeover.

A takeover can be effected in two ways:

- A contractual takeover offer whereby the bidder makes an offer to the target shareholders which is subsequently accepted by over 50% of the voting shares. If 90% of the voting shares accept the offer the buyer may be able to acquire the remaining shares from the minority. This method is more flexible than a scheme (see below) and can be implemented in a shorter period of time.
- A scheme of arrangement whereby 75% of the voting shares agree to the take over which is also approved by the High Court. In these circumstances all of the shareholders will be bound. This method will generally be used to implement recommended bids and is a more efficient way of acquiring 100% control of the target company.

## 2.2 Primary Regulators

**UK City Code on Takeovers and Mergers**

The EU Takeover directive was implemented in the UK under the terms of part 28 of the Companies Act 2006 and within the City Code on Takeovers and Mergers (the "Code"). The Code provides the framework for public company takeovers in the UK and its objectives include ensuring that target shareholders are treated fairly and not denied the opportunity to consider the merits of a bid, and that they are afforded equivalent treatment by a bidder

The Code is administered by the Panel on Takeovers and Mergers (the "Panel") which has full jurisdiction to enforce the Code and place sanctions for non-compliance. The Panel regulates takeover bids and other merger transactions for companies with registered offices in the United Kingdom, the Channel Islands or the Isle of Man if any of their securities are admitted to trading on a regulated market or multilateral trading facility in the United Kingdom or on any stock exchange in the Channel Islands or the Isle of Man. The Panel comprises of 36 members; 12 of whom are appointed by large financial and business organisations.

**Other Statutory Restrictions for Takeovers**

- Companies Act 2006 – Merger relief which prohibits unlawful financial assistance and provisions concerning a public company's right to investigate who has an interest in its shares;
- Criminal Justice Act 1993 – Prohibits insider dealing;
- Financial Services and Markets Act 2000;
- Financial Services Act 2012;
- Market Abuse Regulation (Regulation 596/2014); and
- Enterprise Act 2002.

**Other Relevant Regulatory Bodies**

- Financial Conduct Authority;
- Competition and Markets Authority (CMA);
- The European Commission - has exclusive jurisdiction where transactions concern the EU Merger Regulation (EUMR) which regulates M&A at EU level;
- Ministerial departments – may be involved when a transaction is of national interest; and
- Specific industries (such as banks) may have their own regulatory body.

## 2.3 Restrictions on Foreign Investments

Foreign companies are subject only to the same regulations which apply to UK based companies such as the UK merger control regime. Whilst the controls apply equally, intervention may be more likely in the case of foreign investors due to public or national interest. The UK government can intervene from a competition law perspective for public interest under the UK merger control regime as stipulated in the Enterprise Act 2002 or the EU Merger control regime under the EU Merger Regulation. The UK government lowered the legislative thresholds (from GBP70 million to GBP1 million) for intervention to protect public interest for targets involved in activities connected with three areas of the economy namely; goods and services with military or dual use, computer hardware technologies and quantum technologies.

Section 13 of the UK Industry Act 1975 allows the Department for Business, Energy and Industrial Strategy to prohibit an acquisition by a foreign entity of an "important manufacturing undertaking" if there is a perceived risk that change of control would be contrary to the interests of the UK as a whole. These powers were used to consider the acquisition by Gardner Aerospace (a subsidiary of a Chinese aerospace and mining company) of Northern Aerospace in June 2018.

## 2.4 Antitrust Regulations

The Competition and Markets Authority (CMA) undertakes merger control and investigations of mergers not caught by EU Merger Regulation based primarily on thresholds including turnover, asset values and market shares.

Transactions which qualify may be investigated by the CMA in an initial Phase 1 investigation. Where this initial phase determines that the merger could result in the substantial lessening of competition in a market in the UK, the CMA will refer the matter to a Phase 2 investigation.

The Phase 2 investigation may result in a prohibition decision or a decision that the transaction should be allowed to proceed subject to commitments or clearance.

There is no requirement to notify the CMA of a merger prior to implementation, however, a company may want to apply for clearance prior to completion in order to manage any risks.

The secretary of state also has limited powers of intervention if a merger raises a "public interest consideration". These powers relate to specific sectors such as newspaper and media outlets as with the investigation into the Sky – Fox merger.

The EU Merger Regulation provides a mechanism for the control of mergers and acquisitions at a European Level where certain market share or turnover thresholds are met at EU level. The EU commission has an initial 25 working days from notification to reach a decision. The period can be extended to 35 days by the parties the takeover will then be cleared or a Phase 11 investigation will commence which could take a further four to seven months.

## 2.5 Labour Law Regulations

With an asset purchase of a private limited company a buyer must have regard to its obligations under TUPE. Where a relevant transfer is deemed to have taken place, anyone employed will be transferred to the buyer under their existing terms of employment.

Prior to completion of the purchase various steps must be taken in order to inform and consult with the employees in order to avoid any liability such as:

- under TUPE, any changes in the employees' terms of employment are void if the sole or principal reason for the change is the transfer itself, unless the reason for the variation is permitted under the contract or for an economic, technical or organisational reason; and
- dismissals will be automatically unfair if the sole or principal reason for the dismissal is the transfer, unless that reason is an economic, technical or organisational reason.

In respect of public takeovers, the Code sets out a number of obligations relating to employees. This includes providing the employees the following information:

- any possible offer announcement that commences an offer period;
- the offer announcement;
- the offer document;
- any circular sent to the shareholders containing the board's opinion on the offer;
- any post-offer undertaking made by a party to an offer; and
- any announcement (or document which includes the contents of the announcement) which the Panel determines.

The employees must also be notified of the offeror's intentions with regards to:

- the future business and safeguarding of the jobs of employees and management;
- any material changes in the conditions of employment; and
- strategic plans for the two companies and the likely impact on:
  (a) employment; and
  (b) places of business.

## 2.6 National Security Review

The Queen's speech, in December 2019, confirmed the National Security and Investment Bill which is aimed at strengthening the government's existing powers to scrutinise and intervene in takeovers and mergers to protect national security. This followed a consultation carried out in 2018 and a white paper published by the Department for Business, Energy & Industrial Strategy, the key points in the paper being:

- to encourage the notification of investments which may raise national security concerns similar to the US CFIUS process;
- the expansion of the range of circumstances where the government has powers to address national security risks such as the acquisition of more than 25% of shares, gaining significant influence or control (Trigger Events). The objective is to prevent controls being circumvented by gaining control of an asset rather than acquiring the business itself; and
- that the government is expected to increase its resources to monitoring the market to identify any Trigger Events with potential national security implications.

Following a review of a Trigger Event, if it is assessed to be a national security risk then the government will have the power to impose conditions on the transaction to prevent or mitigate any risks or in more some circumstances to block or unwind a transaction. Consideration needs to be given to how the new regime would operate in conjunction with the UK merger control regime, and whether it will be necessary to amend the Competition and Markets Authority (CMA).

# 3. Recent Legal Developments

## 3.1 Significant Court Decisions or Legal Developments

Significant court decisions related to M&A are as follows.

Starbev GP Ltd v Interbrew Central European Holdings BV [2016] EWCA Civ 449 – the issue was whether the seller was entitled to a proportion of the profit when the business was subsequently sold on within three years. The seller was claiming EUR129 million. The SPA set out how the seller's Contingent Value Right was to be calculated and it contained an anti-avoidance clause. The Court of Appeal concluded that the transaction was caught by the anti-avoidance clause on the basis it applied "where the dominant purpose of the transaction was to reduce the seller's Contingent Value Right".

Wood v Capita Insurance Services Ltd [2017] UKSC 24 - this is a leading contract law case where the issue was whether "an opaque provision which ….could have been drafted more clearly" required the seller to indemnify the buyer for compensation the FSA required the target company to pay customers for mis sold products. The Supreme Court found for the seller.

Teoco UK Ltd v Aircom Jerszey 4 Ltd & Anor [2018] EWCA Civ 23 – the SPA provided that claims for breach of warranty must be notified. The buyer's notices were invalid because they did not purport to make a claim or to set out the breaches but merely indicated the buyer had or may have claims. The Court ruled the notices were invalid.

In Zayo Group International Ltd v Ainger & Ors [2017] EWHC 2542 (Comm) – the Court found the buyer's notices to be defective because they did not give a reasonable estimate of the damages claimed as required by the notice clause in the SPA.

In Nobahar-Cookson & Ors v The Hut Group Ltd [2016] EWCA Civ 128, the Court of Appeal confirmed that a notification clause with a contractual time limit was a form of exclusion clause which needs to be carefully considered where there is any ambiguity.

In Hopkinson v Towergate Financial (Group) Ltd [2018] EWCA Civ 2744, the Court of Appeal decided that a notice of an indemnity claim by a buyer was valid under the SPA and the buyer did not need to provide details of the alleged claim or estimate total damages.

Rock Advertising v MWB Business Exchange Centres Ltd [2018] UKSC 24, the Supreme Court decided that a variation clause in a contract which required any subsequent variation to be in writing meant that an oral agreement to vary was void.

Two additional important cases regarding a parent company's liability for the actions of its subsidiary are; Lungowe and others v Vedanta and KCM [2019] UKSC 20 – where the Supreme Court found that 1,826 Zambian villagers could pursue a claim in the UK courts against UK based Vedanta Resources PLC and its Zambian subsidiary. The Court of Appeal refused residents of the Niger Delta region the ability to bring a claim in the UK against UK incorporate Royal Dutch Shell PLC (RDS) and its Nigerian operating subsidiary, which decision will be appealed in the Supreme Court in light of the decision in Lungowe.

BTI 2014 LLC v Sequana SA [2019] EWCA Civ 112 – Court of Appeal decided that a dividend can amount to a transaction at an undervalue under the insolvency rules for the purpose of placing assets out of creditors' reach.

Chudley and others v Clydesdale Bank Plc [2019] EWCA Civ 344 – Court of Appeal confirmed the rebuttable presumption that there is a third-party right where a contractual term confers a benefit on a third party pursuant to the UK Contracts (Rights of Third Parties) Act 1999.

Competition Act 1998: Anti-Competitive Conduct in the Asset Management Sector (Case CMP/01-2016/CA98, 21 February 2019) – first Financial Conduct Authority (FCA) decision under its law enforcement powers under the Competition Act 1998, FCA found that three asset management firms had breached competition law by sharing strategic information bilaterally.

### 3.2 Significant Changes to Takeover Law

The UK departed from the EU on 31 January 2020, this will be the most significant factor leading to changes to merger control regulation. However, changes will only be relevant once the transitional period is over as until then the UK will for the most part be treated as an EU member state and most EU law will continue to apply.

A number of proposed changes to the Code have been introduced pending the expiry of the transitional period, The Takeovers (Amendment) (EU Exit) Regulations 2019 (SI 2019/217) will make the changes required to Part 28 of the Companies Act 2006 to enable the UK takeovers regime to operate outside the EU framework of the Takeovers Directive.

The shared jurisdiction rules will be removed whereby whether the Code will apply to a UK-registered shared jurisdiction company will depend on whether the company satisfies the residency test. Offers for companies that have their registered office in an EEA member state and their securities admitted to trading only on a regulated market in the UK will cease to be regulated by the Panel.

However, given that the Panel has only shared jurisdiction on eight takeovers since 2006 and at the end of 2018 there were only 36 which were capable of being included, it is unlikely these changes will have a significant impact on the market.

## 4. Stakebuilding

### 4.1 Principal Stakebuilding Strategies

In the UK, it is not usual for a bidder to build a stake in the target prior to an offer however it does happen. There are pros and cons associated with stake building, by way of example, stake building could be positive as it could offset shares which might be voted against. On the whole, stake building is regarded as a hard-hitting approach and not therefore favoured in the UK.

### 4.2 Material Shareholding Disclosure Threshold

There is an ongoing disclosure requirement under Chapter 5 of the FCA's Disclosure Guidance and Transparency Rules (DTR) which governs UK companies traded on either a regulated or prescribed market. This obligation is triggered by the percentages of voting rights held, whether directly or indirectly or whether through a financial instrument.

A disclosure must be made when a holding's voting rights exceeds 3% of the total and then every time such voting rights increases or decreases by a whole 1% over 3%. The target must notify a Regulatory Information Service (RIS) as soon as possible and in any event by the end of the trading day following notification from the shareholder. The FCA can impose penalties for breach of the disclosure requirements which can result in penalties including the suspension of voting rights of the shares.

Once a takeover period has commenced the disclosure requirement under Rule 8 of the Code applies. There must then be a disclosure of dealings by parties to the takeover in writing on a daily basis to a RIS.

After the opening position disclosure if a person is interested (directly or indirectly) in 1% or more of any class of relevant securities of an offeror or the target, then a dealing disclosure must be made.

### 4.3 Hurdles to Stakebuilding

The Code imposes certain restrictions on a bidder acquiring a stakeholding which must be adhered to. There are also controls with regards to market abuse prohibited by the Market Abuse Regulations which include insider dealing, where a bidder has information which could place the bidder at an unfair advantage. Insider dealing can give rise to civil and criminal sanctions (Criminal Justice Act 1993).

The FCA has the power to impose unlimited sanctions on any contravention of the MAR including Article 14 (prohibits insider dealing) and Article 15 (prohibits market manipulation). The market abuse regime cannot be diluted by any rules introduced by the company.

### 4.4 Dealings in Derivatives

The trading of derivatives is not fully prohibited however following the 2007/2008 financial crisis; dealing in derivatives is highly regulated. The Financial Services and Markets Act 2000 restricts the carrying on of a regulated activity and making financial promotions unless authorised by the FCA. The MiFID II Directive (2014/65/EU) and Markets in Financial Instruments Regulation (Regulation 600/2014) (MiFIR) imposes further measures on derivatives, including the trading of derivatives in specified regulated markets, increased transparency, greater regulatory oversight with explicit powers to demand information regarding the size and purpose of a position in derivative contracts, etc.

European Market Infrastructure Regulation (EMIR) imposes regulation on "over the counter" derivatives (being those traded directly and not through a regulated market) including an obligation on counterparties to report details of all OTC derivative contracts.

### 4.5 Filing/Reporting Obligations

MiFID II introduced position reporting obligations to facilitate monitoring of compliance with the regime and it requires weekly reports confirming aggregate positions held by various categories of participants. The form and scheduling of those reports are specified in Commission Implementing Regulation (EU) 2017/1093 (ITS 4) and Commission Implementing Regulation (EU) 2017/953 (ITS 5). European Securities and Markets Authority (ESMA) will publish the weekly reports online.

EMIR has also imposed reporting requirements to ensure transparency amongst derivatives markets, namely:

- information on each derivative contract must be reported to trade repositories and sent to supervisory authorities; and
- trade repositories are required to publish aggregate positions based on class of derivatives, for OTC and listed derivatives.

### 4.6 Transparency

There is no requirement for a bidder to make known the purpose of its acquisition and its intention regarding control of the company.

## 5. Negotiation Phase

### 5.1 Requirement to Disclose a Deal

An announcement must be made where:

- there is a firm intention to make an offer notified to the target board, the Code governs the requirements for a firm offer announcement (Rule 2.7); or
- there is an acquisition of shares which results in an obligation to make a mandatory offer.

An announcement may have to be made subject to Panel consultation where:

- the target is subject to rumour and speculation; or
- the is unusual movement in the targets share price.

Negotiations or discussions relating to a possible offer are to be extended to a wider group.

### 5.2 Market Practice on Timing

Market Practice on timing for disclosure strictly follows the requirements of the Code. As non-compliance is considered seriously by the Panel.

### 5.3 Scope of Due Diligence

Generally, the due diligence conducted will fall into three main areas for a private limited company:

- Business – considering the boarder market issues such as competitors, business strengths and weaknesses, sales and marketing;
- Financial – identifying the financial risks and opportunities of the business; and
- General/legal – identifying any areas of risk to the buyer as well as providing the buyer with a more comprehensive view of the company in its entirety.

In contrast on a public acquisition, all persons with confidential information on an offer must keep the information confidential until the offer is announced publicly, therefore, due diligence, in the first instance, is limited compared to private sales. The offeror is under a duty to only announce an offer when it knows it will implement the offer (Rule 2.7 of the Code).

### 5.4 Standstills or Exclusivity

To protect target shareholder value, the Code generally prohibits the bidder and target from entering into exclusivity agreements. However, the target can seek safeguards from the bidder which are not prohibited by the Code; see **6.7 Types of Deal Security Measures**.

### 5.5 Definitive Agreements

Tender offer terms and conditions are, generally, set out in the bidder's formal offer or in the Scheme document.

## 6. Structuring

### 6.1 Length of Process for Acquisition/Sale

The timeline for completing a public takeover is broadly as follows whether it is by Offer or Scheme:

- within 28 days (and no earlier than 14 days without the target board's consent), of an announcement of a firm offer, the offer documents must be sent the shareholders (Offer Date);
- the Offer can be closed 21 days from the Offer Date;
- the offeror must announce the level of acceptances and will usually announce the next closing date 22 days after the Offer Date;
- an Offer will become unconditional as to acceptance 60 days after the Offer;
- on the basis the offer becomes unconditional as to acceptances on day 60, 81 days from the Offer Date is then last day for fulfilment of the other conditions. Thereafter 95 days after the Offer Date is the last date for consideration to be posted to the shareholders; and

- the offeror can complete compulsory acquisition procedure 100 days after the Offer Date.

### 6.2 Mandatory Offer Threshold
Rule 9 of the Code provides if a person acquires an interest in shares in the target which results in the person holding 30% or more of the voting shares of that company or person who already holds between 30% to 50% of the voting rights acquires an interest in any other voting shares, that person will be obliged to make an offer to acquire all of the equity and voting share capital of the target on the terms set out within Rule 9.

The offer is to be made in cash (or cash alternative) which is level with the highest price paid by the offeror for any interest in shares in the previous 12 months. The offeror is not entitled to attach any condition to the offer save that where it is refused on the grounds of competition.

### 6.3 Consideration
In 2019, 79% of firm offers were solely cash offers, 15% were solely share offers and 3% were cash and share offers. The remaining 4% involved alternative cash/cash structures.

### 6.4 Common Conditions for a Takeover Offer
The Code permits an offeror to include conditions or indeed pre-conditions to an offer, however, there are constraints, primarily that such conditions must not be dependent on the subjective judgment of the offeror. Common conditions include:

- where consideration shares are going to be issued and such class of shares are already listed as consideration then a condition will be included such that the offer becomes unconditional only once the consideration shares are admitted to listing and to trading;
- that there will be no reference made to the Competition and Markets Authority or, where the takeover falls within the scope of EU Merger control, the European Commission;
- that all relevant authorisations/approvals for conducting the business are in full force and effect at completion;
- there being no material ligation or other disputes ongoing or pending against the target; and
- there being no material adverse changes in the target's financial or trading position other than those which have been made known to the offeror; however, a change in economic, industrial or political circumstances will not normally justify the withdrawal of an offer according to the Panel.

### 6.5 Minimum Acceptance Conditions
Under Rule 10 of the Code, an offeror must have agreed to acquire 50% of the voting rights in the target for it to be able to declare the offer unconditional as to acceptance. An offeror will often include a conditional threshold so that 90% of the shares to which the offer relates must accept. This allows the offeror to rely on s976 of the Companies Act 2006 to acquire the remaining 10% of the shares. Without the 90% condition the offeror will be left to contend with minority shareholders remaining in the company who it will have no right to buyout.

### 6.6 Requirement to Obtain Financing
Generally, an offer cannot be made conditional on obtaining finance; this is reflected within General Principle 5 and Rule 2.7 of the Code. Only in limited circumstances may the Panel permit obtaining finance as a pre-condition to the offer under Rule 13, for example, where it will take a substantial length of time to gain regulatory clearance or authorisation. A bidder must, therefore, ensure it has the funds to satisfy the consideration due in its offer.

### 6.7 Types of Deal Security Measures
There is a general prohibition on "offer-related arrangements", between a bidder and target company on takeovers of UK companies to which the Code applies. Pursuant to Rule 21.2 of the Code, the target company may not enter into any "offer-related arrangement" with the bidder during an offer period or when an offer is reasonably in contemplation without the prior consent of the Panel.

This prohibition covers any agreement, arrangement or commitment in connection with an offer, including any inducement fee arrangement or break fees. Some break fees are permitted, however, where they do not exceed 1% of the offer value and the target's financial adviser has confirmed it is in the best interest of the shareholders.

The following are examples of safeguards permitted under the Code:

- confidentiality constraints;
- non-solicitation of employees, customers or suppliers;
- requirement for assistance for the purposes of obtaining any official authorisation or regulatory clearance;
- employee incentive arrangements; and
- agreement in relation to the future funding of any pension scheme.

### 6.8 Additional Governance Rights
If a bidder does not seek 100% ownership of a target, there is no real scope for the bidder to seek additional governance rights from the target.

### 6.9 Voting by Proxy
Section 324(1) Companies Act 2006 sets out a statutory right of the members to appoint proxies to exercise all or any of the member's rights to attend, speak and vote at general meetings.

This will override any conflicting provision in the company's articles, though the articles will usually prescribe how a proxy is to be appointed.

### 6.10 Squeeze-Out Mechanisms

An offeror can rely on Section 979 of the Companies Act 2006 in order to force minority shareholders into the transaction. This provision is subject to there being a "Takeover Offer" for the purchase of all of the shares in the target company (less the shares already held by the offeree). The offeror must also have acquired or agreed to acquire 90% of the shares which are not currently held by the offeror.

If the above conditions are met, the offeror can give a squeeze out notice under s981 (Companies Act 2006) within three months of the expiry of the original offer to the shareholder who did not accept the original offer ("Minority Shareholders"). The notice will obligate the offeror to acquire the shares from the Minority Shareholders on the same terms of the main takeover offer. The Minority Shareholders can apply to Court to contest the compulsory acquisition, however, the Court is likely to find that the offer the majority shareholder have accepted is fair and reasonable.

Six weeks after serving the squeeze out notice the offeror must provide to the target company a copy of the entire squeeze out notices, a stock transfer form executed by a person nominated by the target in respect of the Minority Shareholder and the consideration for the shares.

### 6.11 Irrevocable Commitments

Irrevocable commitments are widely used to improve the chances of success of a takeover offer. In advance of the announcement of an offer and with the consent of the Panel, shareholders will give an undertaking that they will accept the offer and will vote in favour of any resolutions in order to progress the offer.

There are two types of Irrevocable Commitments, hard irrevocables which are binding even if a higher offer is made or soft irrevocables which will fall away if a higher offer is made. Usually, the higher offer must be at least 10% higher.

If an offeror obtains an irrevocable commitment during the offer period, this must be disclosed in writing to a Regulatory Information Service (RIS) (Rule 2.10(a) of the Code).

## 7. Disclosure

### 7.1 Making a Bid Public

Rule 2.7 of the Code sets out what needs to be included within an announcement, namely (not limited to) offer terms, identity of the offeror, details of any existing holding of shares, any conditions, details of any dealing arrangements, a list of documents which must be published on a website and, where there is a cash element involved in the offer, confirmation from the offerors financial adviser that there are sufficient resources to make the offer. Since January 2018, it is at this stage that an offeror must confirm its intentions with regards to the business, employees and pension scheme of target.

The announcement must be published via a Regulatory Information Service. If the announcement is submitted outside normal business hours, it must also be distributed to at least two national newspapers and two newswire services in the UK.

If a leak occurs, the announcement is governed by Rule 2.4 of the Code.

### 7.2 Type of Disclosure Required

It is unlawful for a public offer of transferable securities (including listed shares) to be made in the UK unless a prospectus approved by the FCA (or the competent authority of another EU state) has been issued beforehand, or an exemption applies. The prospectus regime is policed by the Prospectus Regulation (EU) 2017/1129, which sets out a number of exemptions from the requirements to produce a prospectus.

### 7.3 Producing Financial Statements

A bidder is required to produce audited accounts/financial statements for the previous two years of trading.

### 7.4 Transaction Documents

Alongside the main bid documents, a bidder must disclose to the public other material documents including irrevocable commitments, letters of intent, any offer related arrangements, funding details and any other material contracts related to the offer.

## 8. Duties of Directors

### 8.1 Principal Directors' Duties

Directors owe statutory duties enshrined in the Companies Act 2006.

**Duty to Act Within Powers (Section 171)**

If a director is allotting shares with the intention of preventing a takeover bid this is deemed to be acting outside of the confines of the powers and was successfully challenged in Hogg v Cramphorn Ltd [1967] Ch 254.

**Duty to Promote the Success of the Company (Section 172)**

When considering whether to recommend an offer or in the case of competing bids, the directors will need to consider whether a bid is in the best interest of the company. This involves taking a long-term view of the interests of the company. The court is unlikely to disturb a decision unless no reasonable director could possibly have concluded that such action would promote the success of the company.

**Duty to Exercise Reasonable Care, Skill and Diligence (Section 174)**
Generally a committee will be nominated to oversee the day-to-day responsibility of a takeover; the board are still under a duty to monitor the activities of the committee.

**Duty to Avoid Conflicts of Interest and Conflicts of Duty (Section 175)**
In a takeover, conflicts may arise where a director of the target also holds a position in the bidder company or vice versa or if a target director will have a continued role in the group following the transaction. Where a director does have an interest in an arrangement the director will be under a duty to disclose such interest (Section 177).

Directors owe their duties primarily to the company itself and therefore any action is taken by the company usually after a majority of shareholders have voted for action to be taken. Shareholders are unable to take action unless they can prove unfair prejudice or by bringing a derivative claim seeking relief on behalf of the company where the company has a cause of action against a director.

### 8.2 Special or Ad Hoc Committees
Usually, it is common for a committee to be appointed from the outset to deal with urgent issues relating to the takeover.

Where a company is subject to a management buyout or another connected party transaction which could result in a conflict, a special committee consisting of non-conflicting directors should be appointed in order to deal with the transaction (Investment Association Transaction Guidelines).

Independent advisors should be consulted rather than using the company's existing advisors, it is not sufficient to simply establish information barriers.

### 8.3 Business Judgement Rule
Directors' judgment is rarely challenged in the UK Courts and a Court is unlikely to disturb directors' decisions unless no reasonable board could have reached that decision.

### 8.4 Independent Outside Advice
Rule 3 of the Code provides that the target must have an independent financial adviser. The target board must obtain competent independent advice as to whether the financial terms of any offer (including any alternative offers) are fair and reasonable.

The board will usually put together a team of advisors including investment banks (who will act as the financial advisors), brokers, lawyers, accountants and public relation advisors. This is to enable the board to deal with the offer, the substance of the board's advice to the shareholders and how to deal with the offer process.

### 8.5 Conflicts of Interest
See **8.1 Principal Directors' Duties**.

## 9. Defensive Measures

### 9.1 Hostile Tender Offers
Hostile tender offers are permitted in the UK and account for around 12% to 18% of bids, annually.

### 9.2 Directors' Use of Defensive Measures
The use of defensive measures is restricted by the Code. The Code will only apply once an approach has either been made or the board have reason to believe that a bona fide offer might be imminent.

In such circumstances, under Rule 21.1(a) of the Code, the board cannot, without shareholder approval, take any action which may result in any offer or bona fide possible offer being frustrated or in shareholders being denied the opportunity to decide on its merits. This includes: issuing shares, granting share options, disposing of any material assets and entering into agreements outside the ordinary course of business.

The directors are also prevented from taking any action in so far as it puts them in breach of their director's duties owing to the target.

### 9.3 Common Defensive Measures
Urging shareholders to reject an offer is a commonly used defensive measure.

The Board will seek to persuade the shareholders that the price being offered is an undervaluation of the company and that by not engaging in the sale the shareholders will see a greater benefit in the long run. The Board will make this judgment based on financial information with regards to the performance of the company.

A board may also release new information such as business plans and forecasts to reinforce the idea that the long-term gain will outweigh the shareholders cashing out on the offer.

Where shares are being offered as consideration, the board may scrutinise the value of the offeror and will look to discredit its worth.

The board should ensure that where this tactic is employed any information given must be adequately and fairly presented (Rule 19.1)

### 9.4 Directors' Duties

There are two main duties which are key when employing defensive measures. The first is the duty to act in a way the director considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole (s172 Companies Act 2006). Success is determined based on the directors' judgment, however, the act does provide several factors which must be considered including but not limited to:

- the likely consequences of any decision in the long term; and
- the interests of the company's employees.

The second is that the directors must act within their powers (s171 Companies Act 2006) which requires the director to act within the confines of the company's constitution.

### 9.5 Directors' Ability to "Just Say No"

As detailed, in order for directors to comply with their statutory duties they cannot "just say no". They must make a reasonable assessment based on requisite independent advice in order to determine what is in the company's best interests long term. The Code generally allows for target shareholders to decide the outcome of an offer and, provided directors comply with their duties, they are allowed to express their opposition to a bid.

## 10. Litigation

### 10.1 Frequency of Litigation

Litigation is not common in connection with M&A deals in the UK. Generally, commerciality plays a much larger role resulting in most issues being resolved on commercial terms rather than resorting to litigation. The Panel whilst not strictly of judicial standing does play a key role in determination of issues arising during the course of the bid process.

### 10.2 Stage of Deal

If litigation is brought (which is rare), there is no usual stage which is more likely to result in litigation.

## 11. Activism

### 11.1 Shareholder Activism

Mergers and acquisitions activity remains a key focus for activists. Lazard's Shareholder Advisory Group (Lazard) reported that approximately 46% of all activist campaigns in the first half of 2019 had an M&A angle, as activists continue to view these transactions as opportunities to increase returns for members.

### 11.2 Aims of Activists

Increasingly, activists make their demands public by way of open letters, white paper reports, shareholder proposals and proxy contests. The general aim being to focus on issues relating to corporate governance, such as replacing the management team, level of dividend pay-outs, new director appointment of directors and executive compensation.

### 11.3 Interference with Completion

Activists have developed a number of M&A-related strategies to interfere with completion. These strategies include pressuring companies into a merger or acquisition, or ruining deals that would otherwise have proceeded.

A further popular strategy involves campaigning for improved deal terms, commonly referred to as "bumpitrage". This involves the activist acquiring shares in a company that is subject to a takeover bid, and then persuading the other shareholders that the current bid is insufficient and should be renegotiated.

Often, the threat that shareholder approval may not be forthcoming is sufficient to encourage a target board to renegotiate the terms of the deal.

**Hawkins Hatton Corporate Lawyers Ltd** is a niche corporate law firm based in Dudley and London, dealing primarily with corporate and commercial work and commercial property and litigation. Clients include European and Anglo-US companies, regional and national clients and individuals, and include a number of banks, notably RBS, Lloyds, HSBC and Santander, and a large number of small and medium-sized enterprises. Hawkins Hatton provides a full range of company and commercial services. It is known for private equity work for management teams, management buyouts, sales, mergers, acquisitions and disposals for shareholders of small and medium-sized enterprises, and a broad range of corporate work, including restructuring of companies and related tax issues. Services include drafting of sale and purchase agreements, tax deeds and ancillary matters. Commercial contract expertise includes agency and distribution, franchises, guarantees, joint ventures, partnerships, shareholder agreements, terms of business and mortgage securitisation.

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