UK Takeover Code – Developments Over the Last 12 Months

12 September 2017

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Introduction

On 12 September 2016, the UK Takeover Panel published the twelfth edition of the Takeover Code, replacing in its entirety the previous edition published in September 2011 in the wake of Kraft's takeover of Cadbury (**Client Memorandum on New Edition of the Takeover Code**).

The twelfth edition of the Code consolidated rule changes and guidance relating to, among others, profit forecasts and quantified financial benefits statements, post-offer undertakings and intention statements and the communication and distribution of information during an offer.

Since then, there have been a number of key developments relating to the Code and its interpretation.

Specifically, the Panel has published a number of statements and consultation papers in relation to:

- strategic reviews, formal sale processes and other circumstances in which a company is seeking potential offerors (**Practice Statement No. 31** and **Panel Statement 2017/12**);
- Rule 2 on secrecy, possible offer announcements and pre-announcement responsibilities (**Panel Statement 2017/6**);
- asset sales in competition with an offer and other matters (**Panel Consultation Paper 2017/1** and **Panel Statement 2017/13**); and
- the Panel's checklists and supplementary forms (**Panel Statement 2016/9**).

In addition, the Panel has published interesting decisions by the Hearings Committee to cold shoulder Mr. Bob Morton and Mr. John Garner as a result of their behaviour concerning Hubco Investments (**Panel Statement 2017/1**) and dismissing an appeal by Mr. Dave King of a Panel decision requiring a Rule 9 offer to be made for Rangers International FC (**Panel Statement 2017/4**).

There have also been a number of relevant English court decisions on the use of a scheme of arrangement to effect a takeover, including notably in the context of Sainsbury's acquisition of Home Retail Group and Home Retail Group's related disposal of Homebase, ABInBev's acquisition of SABMiller and Severn Trent's acquisition of Dee Valley Group.

Changes to the Code and Practice Statements

Strategic reviews and formal sale processes

On 7 July 2017, the Panel published Practice Statement No. 31 (*Strategic reviews, formal sale processes and other circumstances in which a company is seeking potential offerors*).

Specifically, this statement describes the way in which the Panel normally interprets and applies Rules 2, 21.2 and 21.3 where a target company wishes to announce a strategic review of its business, conduct a formal sale process or to seek a potential offeror.

Practice Statement No. 31 also incorporates the relevant contents of Practice Statements No. 3 (*Controlled auctions*) and No. 6 (*Strategic review announcements*) with minor amendments. Both of these Practice Statements have now been withdrawn.

Strategic reviews

If a target's strategic review announcement refers to an offer, a formal sales process or a search for a buyer (a "formal sales process") as options to be considered, the Panel will normally treat such announcement as commencing an offer period.

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As a consequence, such announcement should identify any potential offeror which has made an approach or with which the target is in talks and specify the 28-day deadline for such potential offeror to announce a firm intention to make an offer (as required by Rule 2.4 and Rule 2.6) unless the strategic review also incorporates a formal sale process in relation to which the Panel has granted a dispensation from such requirements. It is worth noting that the Panel's annual report for 2016/2017 states that 13 offer periods commenced in financial year 2016/2017 with the announcement of a formal sale process.

If the strategic review announcement does not refer to a formal sales process, the Panel will not treat the announcement as automatically commencing an offer period. In such circumstances the Panel will ask the target's advisers on the options being considered by the target's board.

The Panel will normally require the target to make a further announcement, identifying that an offer is an option to be considered under the strategic review where both an offer is being, or will be actively considered and there is rumour about a possible offer or an untoward movement in the target's share price.

Any such further announcement will commence an offer period. Similarly, such announcement should identify any potential offeror which has made an approach or with which the target is in talks and specify the 28-day deadline for such potential offeror to announce a firm intention to make an offer unless the strategic review also incorporates a formal sale process in relation to which Panel has granted a dispensation.

If the conclusion of the strategic review is not to pursue an offer, the target should update the position promptly by way of an announcement.

Amendments to Practice Statement No. 3

In Practice Statement No. 31, the Panel made a minor amendment to the contents of Practice Statement No. 3 to confirm its view that the announcement of a formal sale process will be treated as equivalent to the announcement of the existence of a potential offeror to which information has been given. Accordingly, under Rule 21.3, following such announcement, any information passed to any potential offeror in the process must, on request, be passed to a bona fide potential competing offeror, even if such competing offeror is not participating in the formal sale process.

Amendment to Practice Statement No. 6

The Panel also made a minor amendment to the contents of Practice Statement No. 6 to confirm its view that if, at the time a strategic review announcement which refers to an offer is made, the target is not in talks with any potential offeror and is not in receipt of any approach, this should be stated in such announcement.

Secrecy, possible offers and pre-announcement responsibilities

On 13 April 2017, the Panel published an amended Practice Statement No. 20 (*Rule 2 – Secrecy, possible offer announcements and pre-announcement responsibilities*). The key amendments made to this statement were as follows:

- the statement now clarifies that the requirement to consult the Panel before more than six parties is approached about an offer or possible offer continues to apply during an offer period in relation to a possible offer by any potential offeror which has not been identified; and
- the statement also states that if a shareholder or other relevant person is approached before the commencement of an offer period and the relevant meeting relates to a possible offer, such meeting will need to be attended by a financial adviser or corporate broker. In addition such financial adviser or corporate broker must by not later than 12 noon the following business day, provide a written

confirmation to the Panel as specified by Rule 20.2(c) or Note 1 on Rule 20.2 (as applicable). Such written confirmation is not required if no representative of, or adviser to, the offeror or target was present other than the financial adviser or broker and no material new information or significant new opinions relating to the possible offer were provided during such meeting.

Consultation on asset sales in competition with an offer

On 12 July 2017, the Panel published Panel Consultation Paper 2017/1 (*Asset sales in competition with an offer and other matters*) on its proposed amendments to the Code in relation to the sale by a target of assets in competition with an offer or possible offer.

The purpose of these proposals is to ensure that an offeror or potential offerors would not be able to avoid the application of certain Code provisions by an asset deal.

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The consultation paper also proposes a number of amendments to the relevant rules on social media and financial advisers, and other miscellaneous matters.

Responses to the consultation should reach the Panel by 22 September 2017.

In particular, the Panel is proposing that:

- Rule 2.8 be amended to prevent a person who has made a "no intention to bid" statement from purchasing, agreeing to purchase or making any statement which raises or confirms the possibility that it is interested in purchasing significant assets of the target, within six months of the date of such statement except in certain circumstances or with the Panel's consent.
- Rule 12.2(b)(i) be amended to prevent an offeror or its concert parties from purchasing, agreeing to purchase or making any statement which raises or confirms the possibility that it is interested in purchasing significant assets of the target during a competition reference period except with the Panel's consent.
- Rule 35.1 be amended to prevent an offeror or its concert parties, where an offer has been announced or made but has not become or been declared wholly unconditional and has been withdrawn or has lapsed otherwise than pursuant to Rule 12.1 in relation to competition references or proceedings, from purchasing, agreeing to purchase or making any statement which raises or confirms the possibility that it is interested in purchasing significant assets of the target, within twelve months from the date on which such offer is withdrawn or lapses except with the Panel's consent.

- New notes be added to Rule 2.8, Rule 12.2, Rule 35.1 to provide that in assessing whether such assets are significant for the purposes of these rules, the Panel would have regard to the:
  - aggregate value of the consideration for the assets compared with the aggregate market value of all the target's equity shares;
  - value of the assets to be purchased compared with the total assets of the target (excluding cash and cash equivalents); and
  - the operating profit attributable to the assets to be purchased compared with that of the target,

  and relative values of more than 50% will normally be regarded by the Panel as significant.
- A new note be added to Rule 2.8 to provide that where a "no intention to bid" statement is made by a potential offeror which has previously made an unqualified statement regarding the terms on which it might make an offer and did not reserve the right not to be bound by that statement with the target board's agreement, the target board may not agree to the restrictions in the proposed amendments to Rule 2.8 (as set out above) being set aside for three months following the date on which such potential offeror makes such statement.
- Rule 21.1, which imposes certain restrictions on actions which may result in any offer being frustrated or in a target's shareholders being denied the opportunity to decide on such offer's merits, be amended to:
  - make clear that shareholder approval will not be required if the taking of the proposed action is conditional on the offer being withdrawn or lapsing;
  - require that, where shareholder approval is sought for a proposed action under Rule 21.1, the target board must obtain competent independent advice on whether the financial terms of the proposed action are fair and reasonable and the Panel must be consulted regarding the date on which the relevant shareholder meeting is proposed to be held;
  - require that, where shareholder approval is sought or would be sought but for the fact that the taking of the proposed action is conditional on the offer being withdrawn or lapsing, the target board must send a circular to shareholders containing certain specified information; and
  - permit a target to enter into an agreement to pay a *de minimis* inducement fee to a counterparty to a transaction to which Rule 21.1 applies.

- Where in competition with an offer or possible offer, a target's board is proposing to sell all or substantially all of the target's assets and to return to shareholders all or substantially all of the target's cash balances:
  - a new note be added to the definition of "quantified financial benefit statement" in the Code to include a statement made by the target's board qualifying the cash sum expected to be paid to shareholders if the offer is withdrawn or lapses within such definition;
  - a new Rule 4.7 be introduced to provide that the purchaser of such assets shall not acquire interests in the target's shares during the offer period unless the target board makes a statement quantifying the cash sum expected to be paid to shareholders, and then only to the extent that the price paid does not exceed the amount stated; and
  - a new note be added to Rule 21.3 to provide that the requirement under this Rule that information given to a offeror or potential offeror must be given to another offeror or bona fide potential offeror should be applied also to persons who are interested in purchasing all or substantially all of the target's assets.
- Rule 2.8 and Note 2 on Rule 2.8 be amended to require a person making a "no intention to bid" statement to specify in such statement the circumstances in which it reserves the right to set the statement aside.
- Rule 20.4 be amended to remove the restrictions on the use of social media for the publication of information about a party to an offer and to permit the publication via social media of videos approved by the Panel in accordance with Rule 20.3.
- Note 1 on Rule 19.1 be amended to clarify that financial advisers are responsible for guiding their clients with regard to the publication of information via social media in the same way as for information published by other means.
- Notes on Dispensations from Rule 9 be amended to reflect the practice of the Panel to consider granting waivers from the obligation to make a mandatory offer that would otherwise arise under Rule 9 as a result of an issue of new securities if independent shareholders holding shares carrying more than 50% of a company's voting rights capable of being cast on a "whitewash" resolution give certain written confirmations.

Panel checklists and forms

On 14 December 2016, the Panel published Panel Statement 2016/9 (*New checklists*) prescribing new checklists and supplementary forms to be completed and submitted to the Panel by the financial adviser to the bidder or the target (as appropriate), together with the documents required to be sent to the Panel under Rule 30.5.

Requirements of Rule 30.5

Rule 30.5(a) relates to the distribution of documents, announcements and information to the Panel. Specifically, it provides that before an offer document is published, a hard copy and electronic copy of such document must be sent to the Panel. In addition, Rule 30.5(b) states that copies of all other documents, announcements and information published in connection with an offer by (or on behalf of) the bidder or the target must, at the time of publication, be sent in hard copy and electronic form to the Panel. The Note on Rule 30.5 adds that where information is incorporated into such documents by reference to another source of information, a copy of the information so incorporated should be sent to the Panel at the same time.

Panel Statement 2016/9

Panel Statement 2016/9 prescribes new checklists and supplementary forms to be completed and submitted to the Panel by the financial adviser to the bidder or the target (as appropriate), together with the documents required to be sent to the Panel under Rule 30.5. The checklists relate to:

- firm offer announcements;
- offer documents and offeree board circulars;
- scheme circulars; and
- Rule 15 offers and proposals.

In addition, if an announcement or other relevant document includes a profit forecast, a qualified financial benefits statement, an asset valuation or a partial offer, a supplementary form must be completed by the target's financial adviser and attached to the relevant checklist to be submitted by the bidder's financial adviser.

Both the new checklists and supplementary forms can be downloaded at **www.thetakeoverpanel.org.uk/checklists**.

The Panel has noted that:

- the checklists and forms require advisers to confirm and explain compliance with the relevant provisions of the Code;
- they should be used with immediate effect;
- they are not intended to be used to "pre-vet" announcements or documents; and
- it will continue its existing practice of only pre-vetting "whitewash" circulars and documents sent to shareholders in relation to a proposed re-registration or Code waiver.

Completing the new checklists

Information on how to complete the checklists and supplementary forms and submit them to the Panel is set out on the Panel's website at **www.thetakeoverpanel.org.uk/checklists/how-to-complete**.

The Panel has noted that:

- the checklists and forms should clearly identify where in the announcement or document the relevant information is located;
- if a Code provision is not applicable, the comments column in the checklists and forms should be used to explain briefly why such provision is not applicable;
- the completed checklists must be approved (signed) by a representative of the relevant financial adviser before they are submitted to the Panel;
- by signing the checklist, the financial adviser confirms that:
  - the checklist (and the supplementary forms attached to it) has been completed in accordance with the Panel's guidance on how to complete checklists and supplementary forms as set out on its website; and
  - it is responsible for, and can be contacted in respect of, any aspect of the relevant section of the checklist for which it has approved.

The Panel has also noted that in some instances (e.g., where there is a joint offer document) a checklist may require the signature of the representatives of both the financial adviser to the bidder and the financial adviser to the target.

If so, the Panel expects that only one checklist will be submitted and it is up to the parties to coordinate how this is done.

> By signing the checklist, the financial adviser confirms that the checklist has been completed in accordance with the Panel's guidance

Rule 30.5 documents, together with the checklists and forms, are to be emailed to **documentfiling@thetakeoverpanel.org.uk** and hard copies sent to the Panel as follows:

- offer document or scheme circular (recommended) – eight copies;
- offer document, offeree board circular or scheme circular (unilateral) – 12 copies; and
- revised offer document or offeree board circular – eight copies.

Decisions of the Panel

Cold shouldering: *Hubco*

Cold shouldering

Section 11(b) of the Introduction to the Code states that if the Panel finds a breach of the Code, it may publish a Panel Statement indicating that the offender is unlikely to comply with the Code.

The consequence of such statement is that members of the UK Financial Conduct Authority (FCA) and certain professional bodies would not, in accordance with their respective rules, be able to act for such person in a transaction subject to the Code (i.e., that person would be "cold shouldered").

This penalty is the most serious disciplinary power available to the Panel.

On 10 January 2017 the Panel published Panel Statement 2017/1, in which it declared the "cold shouldering" of Mr. Bob Morton and Mr. John Garner as a consequence of a breach of Section 9(a) of the Introduction to the Code.

The statement is helpful in understanding the Panel's approach to "cold shouldering", as the penalty has been imposed on only two previous occasions – in 1992 and 2010.

Background

On 17 July 2013, Groundlinks Limited, a British Virgin Islands company owned by the trustee for one of Morton's family trusts, acquired shares in Hubco Investments plc, a company admitted to trading on PLUS. In February 2015, Morton became aware that this acquisition may have increased the holdings in Hubco of companies, owned either by trustees of his family trusts or by himself and his wife, to more than 30% of Hubco's issued share capital, thus potentially triggering an obligation to make a mandatory offer to other Hubco shareholders under Rule 9 of the Takeover Code. No such offer was made at the time.

The Panel commenced its investigation into this alleged breach of Rule 9 in April 2015. During a call with the Panel, Morton contended that Rule 9 had not been triggered as the Hubco shares were acquired by Groundlinks on trust for Garner at the time of the acquisition. As Garner was unable to afford the purchase of such shares at that time, Morton informed the Panel that the purchase was funded against a promissory note from Garner to repay the consideration for such shares at a later time.

In May 2015, Garner confirmed this version of the events and informed the Panel that the promissory note had been signed and dated at the time of the acquisition. He then provided the Panel with a copy of the note dated 17 July 2013. In August 2015 the Panel discovered that this note was drafted in March 2015 by Morton's solicitor and that Garner had backdated the note to 17 July 2013. This led to a number of factual retractions by both Morton and Garner on the signing and dating of the note, although they maintained that the relevant Hubco shares were acquired by Groundlinks for Garner as beneficiary.

Panel findings

Section 9(a) of the Introduction to the Code states that the Panel expects parties to deal with it in an open and cooperative way. In dealing with the Panel, parties must disclose all relevant information known to them, and correct or update that information if it changes. Specifically, they must take all reasonable care not to provide incorrect, incomplete or misleading information to the Panel.

In Panel Statement 2017/1 the Panel ruled that:

- the agreement alleged to have been entered into by Morton and Garner on the ownership of the relevant Hubco shares was a lie; and
- Morton and Garner had deliberately attempted to mislead the Panel into believing that there was such an agreement through the production of the backdated promissory note.

Therefore, the Panel decided that Morton and Garner were in breach of Section 9(a), as they had systematically provided the Panel with information which they knew to be false, in order to deceive the Panel into believing that there was no breach of Rule 9 of the Code.

Considering the extent of this breach, the Panel ruled that Morton and Garner are persons who are unlikely to comply with the Code. The Panel ruled that Morton be cold shouldered for six years. It justified this time frame on the basis that Morton's collaboration with Garner in providing the Panel with a "*dishonestly back-dated promissory note*" which purported to acknowledge a transaction that he had invented constituted "*particularly egregious misconduct*". Further, Morton was a repeat offender; he had been disciplined by the Panel on three previous occasions. In 2015, the Panel publicly censured Morton for failing to make a Rule 9 mandatory offer in connection with the purchase of shares in Armour Group plc by his four sons in 2011.

They had systematically provided the Panel with information which they knew to be false, in order to deceive the Panel into believing that there was no breach of Rule 9

Morton's counsel had argued that the penalty was too harsh as the case did not involve a breach of Rule 9. Morton (together with persons acting in concert with him) held more than 50% of the Hubco shares at the relevant time and, therefore, was not under an obligation to make a Rule 9 offer. In response, the Panel noted that detriment to others is only one of many criteria which the Panel may take into consideration when exercising its disciplinary powers. As it is vital to the efficacy of the UK takeover regime that persons act honestly and in good faith with the Panel, the Panel ruled that Morton should be cold shouldered as a deterrence to others.

Regarding Garner – who will be cold shouldered for two years – the Panel noted that it had considered whether it could impose a different penalty. Garner's counsel had argued that his misconduct was out of character and his business career was at a relatively early stage. The Panel concluded that it was unable to impose a different penalty, as Garner's role in

misleading the Panel was significant. Specifically, he had signed and dishonestly backdated the note for a fictitious debt.

FCA statement

After Panel Statement 2017/1 was published, the FCA issued a statement to remind all regulated firms that – in accordance with MAR 4.3 (*Support of the Takeover Panel's Functions*) of the FCA Handbook – they should not deal with Garner, Morton or their principals on any transactions applicable to the Code. In addition, the FCA stated that it expects regulated firms to inform all their approved persons that they should not deal with these individuals on such transactions. The FCA added that a breach of MAR 4.3 may leave a firm and any individuals exposed to enforcement action by the FCA.

Acting in concert: *Rangers*

On 13 March 2017, the UK Takeover Appeal Board published its decision on whether interests in Rangers International Football Club PLC's shares carrying more than 30% of its voting rights were acquired by certain persons "acting in concert" so as to trigger an obligation to make a mandatory Rule 9 offer.

Background

On 31 December 2014, Mr. George Letham, Mr. George Taylor and Mr. Douglas Park acquired interests in Rangers from Laxey Partners Limited. Following such acquisition, and taking into account shares already held by Taylor, the shares held by the three men amounted to 19.48% of the issued shares in Rangers.

Mr. Dave King was also interested in acquiring interests in Rangers shares. However, as King was aware that Laxey was unwilling to sell its Rangers shares to him, he took steps to acquire them from other shareholders. On 31 December 2014, King instructed Cantor Fitzgerald, an investment bank, and on 2 January 2015, he completed his purchase of 14.57% of the issued shares in Rangers.

In accordance with King's instructions to Cantor Fitzgerald, the shares were acquired by New Oasis Asset Limited. New Oasis is wholly owned by Sovereign Trust International Limited, which, in turn, is a trustee of the Glencoe Investments Trust, a trust established by King for the benefit of himself and members of his family. The assets of such trust include a share in New Oasis.

Letham and King had been in touch with each other from the summer of 2014 onwards. In October 2014, they co-operated in two unsuccessful proposals concerning Rangers. The first would have resulted in an acquisition of 33% of the Rangers' share capital, and the second involved acquiring a blocking stake of 25% in Rangers shares. Following the failure of these two proposals, Letham and King continued to stay in touch.

The Panel Executive began to investigate allegations that King had acted in concert with Letham, Taylor and Park in early 2015.

In aggregate, their holdings were then 34.05% of Rangers' issued shares. On 20 July 2015, the Panel Executive informed the parties that it had reached the preliminary view that they were acting in concert and King was the principal member of that group. All the parties denied that they had acted in concert. On 7 June 2016, following further investigations and interviews, the Panel re-asserted its position, and concluded that an obligation should be imposed on King to make a mandatory Rule 9 offer.

King requested a review of the Panel Executive's ruling by the Hearings Committee. A hearing was held on 28 November 2016 and in its ruling on 5 December 2016, the Hearings Committee upheld the Panel Executive's decision. King then submitted a notice of appeal to the Appeal Board.

Takeover Appeal Board findings

King had contended that the shares alleged to have been acquired by him were in fact held and acquired by New Oasis. However, the Appeal Board concluded that New Oasis' holding of these shares does not assist King in his appeal. Specifically, paragraph (5) of the definition of "acting in concert" in the Code states that "*a person, [that] person's close relatives, and the related trusts of any of them, all with each other*" are presumed to be acting in concert. Accordingly, by virtue of this presumption, the Appeal Board concluded that New Oasis, Sovereign Trust and Glencoe Investments Trust are presumed to have acted in concert with King and, via King, with Letham, Taylor and Park.

The definition of "acting in concert" in the Code also deems a person to be acting in concert with an "affiliated person" which includes "*any undertaking in respect of which any person… has the power to exercise, or actually exercises, dominant influence or control*". The Appeal Board noted that, in negotiating for the shares and instructing that the shares be put in the name of New Oasis, King communicated with others and acted as if New Oasis, Sovereign Trust and the Glencoe Investments Trust were under his control in relation to the Rangers shares. King was therefore acting in concert with them.

The Appeal Board then addressed the question whether King was acting in concert with Letham, Taylor and Park when the shares in Rangers were acquired on 31 December 2014 and 2 January 2015. On this issue the Appeal Board upheld the ruling of the Hearings Committee. Specifically, the Appeal Board makes clear that there are many ways in which persons may act in concert and that the nature of "acting in concert" calls for a wide definition to cover, for example, "*tacit understandings […] between persons co-operating to purchase shares in a company in order to obtain control of it*".

Direct evidence of what has passed between alleged concert parties is rare, and that the determination of whether persons have acted in concert often calls for the use of common sense and relevant experience in making reasonable inferences from all the surrounding circumstances

The Appeal Board further highlights that direct evidence of what has passed between alleged concert parties is rare, and that the determination of whether persons have acted in concert often calls for the use of "*common sense and relevant experience in making reasonable inferences from all the surrounding circumstances*". Those circumstances include the personal and working relationships between the parties.

On the case in question, the Appeal Board concluded that there is in fact evidence of contemporaneous emails passing between King and Letham, and that these emails, when read in the context of their earlier co-operation in activities concerning Rangers, are material to the determination of whether the relevant acquisitions of shares were indeed concerted. Accordingly, the Appeal Board ruled that King had acted in concert with Letham, Taylor and Park in the acquisition of over 30% of the issued shares in Rangers. Since King is the principal member of the group of persons acting in concert within the meaning of Rule 9.2, he was under an obligation to make a mandatory Rule 9 offer.

Relevant caselaw on schemes of arrangement

Cancellation schemes and stamp tax: *Home Retail Group*

In *Re Home Retail Group plc [2016] EWHC 2072*, the High Court considered whether a cancellation scheme connected to a takeover fell within the anti-avoidance provisions in section 641(2A) of the Companies Act 2006.

Facts

On 18 January 2016, Home Retail Group plc announced that it had agreed to sell Homebase, its DIY retail business, to Westfarmers and that it would make a capital return to its shareholders of the net cash proceeds of such sale. Prior to the completion of such sale, Home Retail and J Sainsbury plc reached an agreement on the takeover of Home Retail by Sainsbury. The consideration offered by Sainsbury took into account such capital return.

In order to effect the takeover, a scheme of arrangement was proposed pursuant to which Home Retail shares would be cancelled and in exchange, Home Retail's shareholders would be issued with shares in a new parent holding company (Newco) in substantially the same proportion as they previously held in Home Retail. The capital return to shareholders in relation to the Homebase sale would then be effected by way of a capital reduction. Subsequently, the shares in Newco would be transferred to Sainsbury to complete the takeover.

Transfer vs. cancellation schemes

Prior to 4 March 2015, two types of scheme of arrangement were typically used to effect a UK public takeover.

A **transfer scheme** effected the transfer of the target's shares from all shareholders to the bidder through the appointment of a third party to execute all necessary documents on behalf of such shareholders.

A **cancellation scheme** involved the cancellation of all of the target's shares by way of a reduction of capital, the application of the reserve arising from such cancellation in paying up a number of new shares in the target and the issue and allotment of such new shares to the bidder.

One important advantage of a cancellation scheme over a transfer scheme (and over a takeover by contractual offer) was that no stamp duty was payable, as a cancellation scheme did not involve a transfer or agreement for the transfer of shares from the target shareholders to the bidder.

Using a cancellation scheme reduced the cost of implementing a takeover by 0.5% of the value of the shares acquired by the bidder in the takeover.

To protect the UK Government's stamp duty base, section 641 of the Companies Act 2006 was amended on 4 March 2015 to prohibit a company from reducing its share capital as part of a scheme where the purpose of the scheme is to acquire all the shares in a company. Section 641(2B) of the Companies Act 2006 goes on to provide that the prohibition does not apply to a scheme under which:

- the company is to have a new parent undertaking;
- all or substantially all of the members of the company become members of the parent undertaking; and
- the members of the company are to hold proportions of the equity share capital of the parent undertaking in the same or substantially the same proportions as they hold the equity share capital of the company.

This exemption is intended to capture corporate reorganisations where the ownership interests in the company remain substantially the same.

Decision

Home Retail sought confirmation from the High Court that the exemption in section 641(2B) of the Companies Act 2006 applied to the proposed scheme given that:

- Home Retail would have a new parent undertaking (i.e., Newco);
- all or substantially all of the members of Home Retail would become members of Newco; and
- their new holdings in Newco would correspond to their previous holdings in Home Retail.

On 4 July 2016, Newey J ruled that there is "*no doubt*" that section 641(2B) applies to the scheme in question if this subsection is read literally. However, he also considered whether or not the Ramsay principle should be applied. Specifically, the Ramsay principle (reaffirmed by the Supreme Court in *UBS AG v HMRC [2016] UKSC 13*) is an approach to statutory interpretation whereby the courts must analyse Parliament's intent behind the relevant legislation and apply such intent to the facts of the case.

Newey J did not come to a firm view on whether the Ramsay principle applied to the Home Retail scheme. Instead he ruled that, regardless of whether or not the Ramsay principle applied, section 641(2B) of the Companies Act 2006 "*will not bite*" on a cancellation scheme which is part of a real world transaction with a clear commercial and business purpose. Since the scheme in question has such purpose, he held that it fell within the exception in section 641(2B).

Class composition: *SABMiller*

In *Re SABMiller plc [2016] EWHC 2153 (Ch)*, the High Court considered whether it had the jurisdiction to summon a scheme meeting under section 896 of the Companies Act 2006 which did not include the two largest shareholders of SABMiller plc.

Facts

On 10 October 2016, Anheuser-Busch InBev SA/NV completed the acquisition of SABMiller for over £79 billion. The transaction was implemented through a three-stage process:

- the acquisition of SABMiller by a newly incorporated Belgian company (Newco) under a UK scheme of arrangement;
- a Belgian law cash offer; and
- a Belgian law merger in which AB InBev merged into Newco – the new holding company for the group.

Prior to the transaction, Altria Group Inc. was SABMiller's largest shareholder with 26.48% of its ordinary share capital and BEVCO Ltd. was the second largest shareholder with 13.85%. Altria and BEVCO had provided irrevocable undertakings to AB InBev to approve the SABMiller scheme. Altria and BEVCO also irrevocably undertook to elect to receive £4.6588 in cash and 0.483969 restricted shares in Newco, rather than £45 in cash. This share alternative had been structured with Altria and BEVCO in mind and both Altria and BEVCO had rights against SABMiller under an existing relationship agreement.

In order to effect the scheme, SABMiller applied to the High Court seeking an order to summon a single meeting of all holders of ordinary shares in SABMiller other than Altria and BEVCO.

This was because there was a legal risk that Altria and BEVCO's rights could be viewed as sufficiently dissimilar to those of the other shareholders, and therefore they would constitute a separate class for the purpose of the vote on the SABMiller scheme. Accordingly, SABMiller proposed to the High Court that Altria and BEVCO be treated as a separate class of shareholders and to allow other SAB Miller shareholders to vote on the scheme separately.

There was a legal risk that Altria and BEVCO's rights could be viewed as sufficiently dissimilar to those of the other shareholders, and therefore they would constitute a separate class for the purpose of the vote on the SABMiller scheme

Soroban was a small shareholder in SABMiller. Whilst Soroban supported the transaction and intended to vote in favour of the scheme, it submitted to the courts that there should only be one class meeting to which all SABMiller shareholders (including Altria and BEVCO) were summoned. This is to ensure that any dissentient members would be outvoted. Specifically, Soroban argued that section 896 does not provide the courts with the power to summon a meeting of only some shareholders with whom a scheme is proposed.

Decision

The High Court held that it had the jurisdiction to order a scheme meeting to be summoned which did not include Altria and BEVCO. Specifically, it rejected Soroban's argument for the following reasons:

- there is nothing in section 896 to suggest that a shareholder cannot voluntarily agree to waive or forgo its right to participate in the scheme meeting (which is what Altria and BEVCO have done); and
- whilst Part 26 of the Companies Act 2006 must be construed so as to prevent the statutory regime from being used so as to result in injustice to dissentient members, where a member is willing to give his consent voluntarily by agreeing to give an undertaking to be bound by the proposal, there is no injustice to him if he is not summoned to a scheme meeting. There is also no injustice to the other members if the consenting member simply agrees not to be included in the scheme meeting. These other members also have no rights to force the consenting member to attend and vote.

Share splitting to defeat a scheme: *Dee Valley Group*

In *Dee Valley Group plc, Re Companies Act [2017] EWHC 184 (Ch)* the High Court considered how to address a deliberate attempt to defeat a scheme of arrangement through share splitting.

Facts

For a scheme of arrangement to be sanctioned there must be approval by a majority in number representing at least 75 per cent. in value of those attending and voting at each class meeting convened by the court. Dee Valley had proposed a scheme of arrangement for the purpose of enabling Severn Trent Water Limited to complete a takeover recommended by the Dee Valley board of directors. At a shareholder meeting convened by the court, 466 out of 828 members present in person or by proxy voted against the resolution to approve the scheme of arrangement meaning that the headcount requirement was not satisfied. However, the chairman of the meeting excluded the votes cast by 434 individual shareholders consisting of an employee of Dee Valley who had split his shareholding by transferring shares by way of gift to 433 other individuals.

Decision

In considering whether it was suitable to sanction the scheme of arrangement the court concluded that notwithstanding that Dee Valley had obtained a court order in advance of the shareholder meeting permitting the chairman to exclude the votes arising from share splitting, the chairman had a discretion to exclude those votes so as to protect the meeting from manipulation. It further concluded that it was in the interests of the class as a whole to exclude the votes arising from the share splitting on the basis that the member of a class must exercise their votes in the interests of the class as a whole which on the facts was not the case since the individual shareholders had joined the class only with the intention of frustrating the completion of the takeover by Severn Trent.

If the court had concluded that the share splitting was permissible then the ability to employ schemes of arrangement in connection with takeovers would have been called into question as a target company register would be open to manipulation by dissentient shareholders.

Looking forwards?

In addition to describing its work on the matters covered in this memorandum, the Panel's **annual report and accounts for the year ended 31 March 2017**, published on 19 July 2017, noted the preliminary work that it had undertaken to understand the extent to which Brexit will require amendments to be made to Chapter 1 (The Takeover Panel) of Part 28 (Takeovers, etc.) of the Companies Act 2006 and their consequent impact on the Code.

The Panel's initial view is that there are relatively few areas of the Code in which amendments would need to be made – they did highlight that they will need to address the concept of "shared jurisdiction" in the Code which is derived from Directive 2004/25/EC of the European Parliament and of the Council of 21 April 2004 on takeover bids.

As the UK heads towards Brexit in 2019, there will likely be further focus on "shared jurisdiction" as well as the shape of the UK's industrial strategy going forwards including the extent to which Government should have greater flexibility to regulate the acquisition of UK public companies by overseas bidders.

If you have any questions regarding the matters covered in this publication, please contact any of the lawyers listed below or your regular Davis Polk contact.

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