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THE CODE COMMITTEE'S REVIEW OF TAKEOVER REGULATION IN THE U.K.

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The takeover of Cadbury plc by Kraft Foods Inc. in early 2010 prompted widespread public discussion about the regulation of UK takeovers. Concern was expressed that it was too easy for a hostile offeror to obtain control of an offeree company and that the outcomes of takeovers, particularly hostile offers, were unduly influenced by the actions of "short term" investors. On 1 June 2010, the Code Committee (the "Code Committee") of the Takeover Panel (the "Panel") issued a public consultation paper (the "Consultation Paper") containing suggestions for amendments to the Takeover Code (the "Code") to address these concerns.

In its formal response to the consultation published on 21 October 2010, the Code Committee has decided to implement certain of the suggested amendments aimed principally at:

- reducing the tactical advantage obtained in recent times by hostile offerors and redressing the balance in favour of the offeree company;
- ensuring greater account is taken of the position of persons affected by takeovers in addition to offeree company shareholders, most notably employees; and
- increasing transparency and improving the quality of disclosure.

Although it welcomed the Code Committee's proposals for seeking to redress the balance between the offeror and the offeree, the UK Government has responded by launching a consultation of its own. The purpose of the Government's consultation is to determine whether more can be done to promote long-term growth rather than short-term financial gain by examining the economic issues underlying takeovers and the corporate law framework governing takeovers. The outcome of this consultation will be keenly awaited to see whether it will result in further changes to the UK takeover regime.

A summary of the amendments proposed by the Code Committee is set out below. The proposed amendments have not yet come into effect and will form the basis of a further consultation paper

expected to be issued by the Code Committee in Q1 2011. Therefore, break fees for example, which the Code Committee has recommended be prohibited, will continue to be permitted until specific rules prohibiting them are introduced following such further consultation. However, it is likely that the Panel Executive will be keeping a closer eye on compliance with certain other existing Rules affected by the Code Committee's recommendations, such as the employee information and other disclosure requirements contained in the Code regarding the Offeror's plans for the offeree and its employees. In addition, put up or shut up deadlines could be shortened. It is expected that the new rules, as adopted following the further consultation, will come into effect in late Spring of 2011.

Subject	Proposed amendment
Restriction of "virtual bids"	Following an approach, any announcement commencing an offer period must name the potential offeror. Except with the Panel's consent or for controlled auctions, the named potential offeror must, within 28 days, either: (a) announce a firm intention to make an offer; (b) announce that it will not make an offer, in which case it will be bound by Rule 2.8 of the Code and potentially be prevented from bidding for up to six months; or (c) apply to the Panel jointly with the offeree for an extension. In exceptional circumstances, before the commencement of an offer period and where, following a private approach, an offeree is subject to an unacceptable level of siege (e.g. because it could then be impeded in the running of its business under the Code rules against frustrating action), the Panel could consider imposing a private "put up or shut up" deadline on the potential offeror. **Rationale:** to provide certainty on the length of the offer process and prevent protracted "virtual bids" which place offerees under siege; reduces incentive for offeror(s) to leak.
Deal protection measures and inducement fees	Except in controlled auctions, offerees will no longer be able to give: (a) inducement/break fees; or (b) save in limited circumstances, undertakings to take action to implement a takeover or refrain from taking action which might facilitate a competing takeover. This prohibition will extend to no shop and exclusivity arrangements as well as matching rights, undertakings by an offeree to inform the original offeror of an unsolicited approach and no information undertakings. To cater for the impact that the change described in (b) will have on agreements by offerees to implement scheme of arrangement takeover offers, the offeree will, in the case of a recommended scheme of arrangement offer, have to implement the scheme in accordance with a timetable agreed with the Panel (subject to the withdrawal of the offeree board recommendation). Permitted undertakings by an offeree will include: (a) maintaining the confidentiality of offeror information; (b) not soliciting the offeror's customers or employees; and (c) providing information necessary to satisfy offer conditions or obtain regulatory approvals. **Rationale:** (a) to strengthen the offeree's position; and (b) to prohibit deal protections which are detrimental for offeree shareholders and deter competing offerors or lead them to offer less favourable terms.

Subject	Proposed amendment
Factors offeree boards may consider in opining on/recommending the offer	The Code will be clarified so as not to limit the factors the offeree board may consider in opining on or recommending an offer. **Rationale:** the Code should not be taken to require offeree boards to consider the offer price as the sole determining factor.
Disclosure of offer-related fees	The following will need to be disclosed: (a) the estimated aggregate fees of each party; (b) a breakdown of the estimated fees of each category of adviser to the parties, including the minimum and maximum amounts payable (i.e. advisers' success/incentive fees will not be prohibited, save to the extent already provided in the Code). Any material changes to the estimated advisers' fees must be announced; and (c) financing fees. Disclosure may be made in a manner that does not reveal commercially sensitive information regarding the offer. **Rationale:** greater transparency and improved quality of disclosure.
Disclosure of financial information on an offeror	The following will need to be disclosed: (a) detailed financial information on an offeror. This will be required in all offers, not just securities exchange offers as has been the case to date; (b) where the offer is material (no guidance has been provided on what would be "material"), a pro forma balance sheet of the combined group and offeror financial ratings, including changes resulting from the offer; and (c) greater details of acquisition debt financing used by the offeror. Offeror debt financing documents will need to be on public display. **Rationale:** improved quality of disclosure and greater transparency for constituents in addition to offeree shareholders, e.g. directors, employees, customers and creditors of the offeror and offeree.
Disclosure of offeror's intentions regarding the offeree company and its employees	Offerors must continue to disclose plans for the offeree's employees, locations of business and fixed assets and will now have to make a negative statement if no such plans exist. Save with Panel consent, unless another period is stated, such statements must hold true for at least one year after the wholly unconditional date. **Rationale:** better quality information will enable all interested constituents to comply with their own obligations and inform offeree shareholders and employees properly.
Views of employee representatives	Offeree boards must inform employee representatives at the earliest opportunity of their right to circulate an opinion on the effects of the offer on employment. The offeree will be responsible for publishing and paying for the opinion. The Code will be amended so as not to prevent the passing of information in confidence to employee representatives. **Rationale:** to improve the ability of employee representatives to make their views known.

The suggested amendments contained in the Consultation Paper which the Code Committee does not "currently" intend to implement are as follows (these include many of the more fundamental suggestions mooted in the Consultation Paper):

Suggested amendment	Rationale for not implementing
Raising acceptance condition threshold above 50% plus one	The 50% plus one threshold is based on the threshold for passing an ordinary resolution (the resolution needed to replace a board). Without an equivalent change in English company law, any change to the Code would be futile. For example: (a) if an offer lapsed when the offeror had obtained more than 50% acceptances but less than the increased threshold, the position of the offeree company board would be unsustainable; (b) an offeror might obtain statutory control of the offeree company by purchasing more than 50% but fail to satisfy the increased threshold, with the result that the offer lapsed; it would have acquired statutory control but accepting shareholders would be denied an exit; and (c) offerors might be prompted to seek control of offeree companies via changes to the board ahead of, or instead of, making an offer for the company.
Disenfranchising shares acquired during the offer period/introduction of qualifying period before shares can carry voting rights/weighted voting rights	Disenfranchising short-term shareholders would be contrary to: (a) the principle of "one share, one vote" and impair the economic rights attaching to the shares; and (b) the principle of equal treatment for all shareholders of the same class enshrined in General Principle 1 of the Code.
Providing protections for offeror company shareholders similar to those afforded to offeree shareholders	Protection of offeror shareholders under the Code is unnecessary given protections afforded by company law, offer director fiduciary duties and the rules of other regulatory authorities, including the UK Listing Authority. It could involve an inappropriate extraterritorial application of the Code to foreign offerors and create an uneven playing field between competing offerors. An offeror shareholder vote requirement could allow easy lapsing of an offer and reduce certainty of delivery of an offer.

Suggested amendment	Rationale for not implementing
Reduction of disclosure threshold from 1% to 0.5%	The Code's disclosure regime was revised recently to provide greater transparency. The Code Committee will continue to monitor the appropriateness of the disclosure threshold.
Reintroduction of restrictions on the speed at which substantial acquisitions of shares can be made	Reintroducing rules equivalent to the Rules Governing Substantial Acquisitions of Shares abolished in 2006 would place an unnecessary restriction on share dealings where control of a company was not passing or being consolidated. These rules restricted the speed at which persons were able to increase a holding of shares and rights over shares between 15% and 30% of the voting rights of a company, 30% being the threshold at which the Code considers control of a company to pass.
Shortening of offer timetable	The maximum period for the publication of offer documents should remain at 28 days since: (a) offer periods are likely to become shorter as a result of the proposed changes to the "put up or shut up" regime described above; (b) it is not normally in an offeror's interests to delay the publication of its offer document; and (c) for a securities exchange offer requiring the production and approval of a prospectus, the offeror is likely to need the full 28 days.
Separate advice for offeree shareholders	The Rule 3 financial adviser's advice to the offeree board, the substance of which is disclosed to offeree shareholders, should be relied upon as being genuinely independent. A requirement for separate advice for shareholders would increase costs without providing any material benefit.
Splitting up of dealing, voting and offer acceptance decisions	The Code Committee will give further consideration to whether proportionate measures could be introduced to enhance transparency where the dealing, voting and offer acceptance decisions attached to a discloseable shareholding have been split between two or more persons.
Disclosure of offer acceptance/scheme voting decisions	Increased transparency in relation to offer acceptance or scheme voting decisions would not provide significant benefits.

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