THE INSTITUTE OF CHARTERED ACCOUNTANTS IN ENGLAND AND WALES

29 September 2009

Our ref: ICAEW Rep 103/09

The Secretary to the Code Committee
The Takeover Panel
10 Paternoster Square
London
EC4M 7DY

By email supportgroup@thetakeoverpanel.org.uk

Dear Sirs

TAKEOVER PANEL CODE COMMITTEE PCP 2009/2
MISCELLANEOUS CODE AMENDMENTS

The Institute of Chartered Accountants in England and Wales is pleased to respond to your request for comments on *PCP 2009/2 Miscellaneous Code Amendments*.

Please contact me should you wish to discuss any of the points raised in the attached response.

Yours faithfully

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THE INSTITUTE OF CHARTERED ACCOUNTANTS IN ENGLAND AND WALES

ICAEW REPRESENTATION

ICAEW REP 103/09

TAKEOVER PANEL CODE COMMITTEE PCP 2009/2 MISCELLANEOUS CODE AMENDMENTS

Memorandum of comment submitted in September 2009 by The Institute of Chartered Accountants in England and Wales, in response to The Takeover Panel Code Committee's consultation paper PCP 2009/2 Miscellaneous Code Amendments published in July 2009

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INTRODUCTION

1. The Institute of Chartered Accountants in England and Wales (the ICAEW) welcomes the opportunity to comment on the consultation paper *PCP 2009/2 Miscellaneous Code Amendments* published by Code Committee of the Takeover Panel.

WHO WE ARE

2. The ICAEW operates under a Royal Charter, working in the public interest. Its regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the Financial Reporting Council. As a world leading professional accountancy body, the Institute provides leadership and practical support to over 132,000 members in more than 160 countries, working with governments, regulators and industry in order to ensure the highest standards are maintained. The ICAEW is a founding member of the Global Accounting Alliance with over 775,000 members worldwide.

3. Our members provide financial knowledge and guidance based on the highest technical and ethical standards. They are trained to challenge people and organisations to think and act differently, to provide clarity and rigour, and so help create and sustain prosperity. The ICAEW ensures these skills are constantly developed, recognised and valued.

4. The ICAEW Corporate Finance Faculty is a network of over 5,000 corporate finance professionals. This response draws on the experience of Faculty members and other associates with significant experience of working on transactions to which the Takeover Code applies.

MAJOR POINTS

Support for the initiative

5. We agree with a number of the changes proposed in PCP 2009/1 but have concerns about the proposed amendments to Note 8 on Rule 9.1 and to Note 4 on Rule 16 and to the proposed new Rule 16.2.

RESPONSES TO SPECIFIC QUESTIONS

Q1: Do you agree with the proposed amendments to Note 8 on Rule 9.1?

6. We note the proposed amendments to Note 8 on Rule 9.1 and, overall are in agreement. However we would like to raise the following points:

7. In clause (a), we consider there is a need for clarity on the ‘relative value of 30%’. In the first instance, 30% of what? For example, is one supposed to take the total value of Company C against the total value of Company B by reference to any of the metrics mentioned, or a proportion of the total value of Company C (that proportion being reflective of the percentage shareholding interest of Company B in Company C) against the total value of Company B – and is the total value of Company B to include Company C (in particular where C has been consolidated into B's accounts). Secondly, is it sufficient to trigger just one of the assets / market value / profit tests for the relative value to be considered significant? Thirdly, has consideration been given as to guidance on the calculation of market value, in particular in the case of a private company? Further, when is the market value to be assessed – should there be a fixed time or should this be over a period?

8. In clause (b), it would be helpful if the Code Committee provided examples of the factors that would typically be taken into account to determine whether securing control of the second company is a “significant purpose” of acquiring control of the first company. This provision has

been drafted in the form of a presumption – how are parties to rebut the determination that a reasonable person would consider the acquisition of the second company as a being a 'significant person'?

9. In addition, one of the key questions we believe is left unanswered by the suggested changes to Note 8 on Rule 9.1 is, if the Executive were to conclude that a Rule 9 obligation has been incurred, how would the minimum price of any such Rule 9 offer be calculated? If there is no easy or definitive answer to this question, what are the key factors that are likely to be taken into account in setting that price? To what extent, if any, should acquisitions of securities in B be relevant in determining what the minimum offer price for C should be? For example, if A acquired shares in B in the previous 12 month period before the mandatory offer was triggered, should the minimum price be set by reference to the market price of securities in C on that date?

Q2: Do you agree with the proposed amendment to Note 2 on Rule 16, the proposed deletion of Note 4 on Rule 16, the proposed adoption of new Rule 16.2 and the Notes thereon, the amendment to paragraph 4 of Appendix 1 and the related amendments referred to above?

PCP section 3 (a) Introduction and background

10. Has the Code Committee considered whether the change to Rule16 should be dealt with in Rules 24 or 25 instead, or at a minimum include a cross-reference to Rule 16 in Rule 24.5 and in note 3 on Rule 25.1. We note, for example, that Rule 24.5 seems to cover very similar concepts to those being debated in relation to Rule 16. If the question as to whether offeree management hold shares in the offeree is now less relevant in relation to incentivisation arrangements with such management, would these concepts still best be dealt with in Rule 16?

PCP section 3 (b) Relevance of management incentivisation arrangements to shareholders

11. We note that the Code Committee is suggesting that the changes go beyond management incentivisation to the question of the independence of offeree directors in giving their views on an offer. If that is the case, should this concept be caught rather in the Notes on Rule 25.1 or at least a cross-reference be made to Rule 16 and the potential impact of special arrangements on the independence of offeree directors? Also, if the independence of offeree directors is potentially a concern, does the Code Committee have a view as to when such arrangements would likely compromise the independence of offeree directors where, for example, the offer is not an MBO or similar transaction as envisaged by Note 4 on Rule 25.1?

12. We disagree with the Code Committee's view that the concern expressed in paragraph 3.6(b) is one that the Code should seek to regulate. We are of the opinion that, as a general principle, it is for the bidder to decide the value of the offer it wishes to make to shareholders and the level of management arrangements that it considers it should implement going forward. There is a long-established requirement for the Rule 3 adviser to assist the target board in assessing whether the value of any offer is fair for shareholders and, in cases where management are either directors or shareholders, we are open to extending the requirement for Rule 3 adviser comment on whether management incentive arrangements are appropriate taking account of a range of factors. However in line with our comments on PCP section 3 (f) below, we do not consider that the apportionment of value betweeen offer consideration and management incentive arrangements is something that Rule 3 advisers should be required to consider in forming their opinion on the impact on shareholders.

PCP section 3 (c) Relevance of shareholdings

13. Consistent with the view expressed in paragraph 12 above, we believe that the appropriateness of management incentive arrangements should be considered only where management comprise directors and/or shareholders.

PCP section 3 (d) Nature of incentivisation

14. How does the amended Rule 16.2 intend to deal with situations where the offeree (or its remuneration committee on the offeree's behalf) agrees to changes in employment arrangements with offeree management (including changes that might prima facie be caught under Notes 6,7 and/or 8 of Rule 21.1) where the offeror is then asked to 'bless' such changes under Note 1 to Rule 21.1, in order to avoid the potential for such changes to constitute frustrating action? Would such 'blessing' then be treated as a special arrangement involving the offeror to which Rule 16 applies? If so, should a cross reference be made in Rule 21.2 to confirm the relevance of Rule 16 in this regard? Indeed, what impact or relevance, if any, does the Code Committee consider should arise or be placed where the Remuneration Committee of the offeree (and not the individual management members themselves) have been responsible for negotiating the incentivisation packages? Should this simply be a matter of disclosure? Should it be relevant when financial advisers are determining whether consultation with the Executive is relevant (on the basis that potentially in these circumstances the package is not 'unusual either in the context of the relevant industry or best practice')?

PCP section 3(e) Relevance of "management"

15. The cumulative effect of the changes suggested in sections 3(c) to 3(e) would appear to result in a very wide range of incentivisation arrangements being caught, whether or not involving equity in the offeror (which could include relatively innocuous changes to employment terms of offeree management) and whether or not offeree management hold shares in the offeree. The result may be to significantly extend (a) the number of individuals caught by the rule (b) the number of arrangements and (c) the number of different discussions in relation to such arrangements. A Rule 3 adviser would then need to review all of those various arrangements and discussions and potentially provide a fair and reasonable opinon in relation to some but not others, depending on the point reached in the various discussions. A summary of the various discussions would also need to be disclosed.

16. We believe the definition of management is vague and, at worst, too wide and wonder whether the effect of such a wide definition would be overburdensome. We consider that such incentivisation arrangements with management (who are not offeree directors) will only be relevant for the purposes of Rule 16 if such management are high end/ highly paid management who hold offeree shares and would be caught under the definition of Persons Discharging Managerial Responsibilties (PDMR) in section 96B of the Financial Services and Markets Act 2000; namely:

    - a senior executive of an issuer who:
        - has regular access to inside information relating, directly or indirectly, to the issuer;
        - has power to make managerial decisions affecting the future development and business prospects of the issuer; and
        - whose total remuneration (excluding any proposed special arrangements) exceed that of the median of executive board members.

    An alternative to the formulation in the third bullet point above would be to capture persons 'whose total remuneration (excluding any proposed special arrangements) represents at least [75]% of the highest paid member of the executive board of the company'.

PCP section 3(f) The opinion of the offeree company's independent adviser

17. According to paragraph 3.14 the Code Committee considers that advisers should, in particular, bear in mind the concerns referred to in paragraph 3.6. We consider that the requirement to consider paragraph 3.6 (b) is too onerous. Instead we believe that in commenting on whether proposed management arrangements are fair and reasonable so far as shareholders are concerned, Rule 3 advisers should consider whether the arrangements are in line with industry norms for the deal structure, the nature and size of the business, the bidder's policy for rewarding key executives, the target's existing arrangements for the people concerned, the views of the target's remuneration committee and whether the proposed arangements are being put in place properly to incentivise management. When the Code Committee considers its response to this consultation it would be helpful to have clarification as to the Code Committee's views on the relevant factors it considers a Rule 3 adviser should consider in this regard.

PCP section 3(g) Where no incentivisation arrangements are proposed or the terms of any incentivisation arrangements have not been finalised

18. In paragraph 3.15 clause (i), has the Committee considered putting a time limit on this requirement (reflecting, for example, the concept caught in Rule 35.3)? In that vein, we consider there is a need for further commentary from the Code Committee on whether the statement could be further qualified by reference to the fact that no incentivisation arrangements are '**currently**' proposed. In addition, a qualification could be made to clause (i) as follows:

    '…save in line with the normal practice of the bidder regarding salary and options.'

19. In paragraph 3.15 clause (ii), we believe there is a risk that the requirement for 'full details of the discussions to be disclosed' will result in generic, boilerplate disclosures. Key matters would normally include: when discussions commenced, who initiated them, who conducted the discussions/ negotiations e.g in particular if done through Remuneration Committee, what where the key factors which impacted on final package e.g. reference to comparative company or reference to internal usual annual increases for other staff.

20. Additionally in paragrah 3.15 clause (iii) it should be recognised that it may be difficult for a party to make an unqualified statement which lasts, in theory, for all time. Accordingly it would be helpful if the Code Committee confirmed whether Rule 3 advisers should consider updating their opinion when arrangements have been finalised and what obligations would apply regarding any updates during an offer period or on publication of any subsequent documents (if applicable).

21. As we mention above, we have also considered the link between the requirements in paragraph 3.15 and Rule 24.5. Is there confusing overlap here and/or might it not be helpful to include a note in Rule 24.5 directing practitioners to the requirements of Rule 16.2(a)?

PCP section 3(h) The requirement to consult the Panel

22. In practice, different Rule 3 advisers or offeree boards are likely to reach different conclusions as to whether 'the value of any arrangement to be entered into….is significant and/or the nature of the arrangement is unusual…' and, therefore, whether they would need to discuss the position with the Executive. We note the Code Committee's stated desire in paragraph 3.5 to achieve a more consistent approach in relation to offeree management incentivisation arrangements but think, in light of the above, that such consistency may well be unachievable. Without a consistent approach from advisers regarding consultation with the Executive, it may not be possible to apply a consistent approach to requiring a shareholder vote. In particular there could be a risk that the Executive may determine after a document has been posted that,

had it been consulted, it would have required a shareholder vote in connection with management incentive arrangements which would be complex to deal with at that late stage.

PCP section 3(i) The Panel's consent and the requirement to seek the approval of independent shareholders

23. We consider that an elaboration on the circumstances where the Panel would not consent to the proposed arrangements would be helpful. In paragraph 3.18 what would constitute "other than rarely"? Are there any circumstances where the Panel would withhold consent irrespective of whether the parties to an offer were very willing to seek shareholder approval? In addition, in which circumstances, other than those governed by Article 3.1 (a) of the European Directive on Takeover Bids, does the Panel expect to require shareholder approval of management incentive arrangements? Again, clarification from the Code Committee in the response statement would be helpful. Moreover, in relation to Rule 25.1, if director arrangements have not been finalised but the Panel considers that shareholder approval is required, should such approval be sought before or after finalisation of the arrangements?

PCP section 3(j) Article 3.1(a) of the European Directive on Takeover Bids

24. Unless it would be problematic, having regard to the European Directive's requirements in relation to such matters, would it not be helpful to explain what interests are included within the concept of "equity interests", otherwise it could result in quasi equity interests being constructed to avoid the need for shareholder approval?

PCP section 3(k) The form of any resolution required

25. We find that the drafting in paragraph 3.23 is slightly ambiguous. Is it the Executive's practice always to permit an offer to lapse if the arrangements caught by Rule 16 are not approved? Or would that only be the case, say for a management buyout, in line with the current application of Note 4 on Rule 16? Depending on the Code Committee's views on how often shareholder approval is likely to be required (questioned above) there could be a more frequent requirement for a shareholder vote. Where the success of a shareholder vote is permitted to be a condition of an offer, we question how valuable this is for shareholders. If shareholders want to get the benefit of the offer they are indirectly forced to vote in favour of the management arrangements where approval is an offer condition. Depending on the answers to those questions, is it worth making some cross-reference to or in Rules 13 and 16 to reflect that approach?

Q3: Should the Code be amended to require display documents to be made available for inspection on a website in addition to hard copy form until the end of the offer (and any related competition reference period)? Do you have any comments on the proposed amendments to Rule 26 or the new Notes 2, 3, 4 and 5?

26. We agree.

Q4: Do you agree the Code should be amended to delete Rule 26(c) as suggested above? Do you agree that Rules 26(d) and (f) should be amended as suggested above?

27. We agree.

Q5: Do you agree that the Note on Rule 2.7 should be amended to make clear that the ability of an offeror to choose not to proceed with an offer where a higher competing offer has been made should be subject to the consent of the Panel?

28. We agree.

Q6: Do you agree that Note 5 on Rule 21.1 should be deleted?

29. We consider it would be better to retain Note 5 on Rule 21.1 but to add a cross-reference to Rule 13.4(a) to clarify that the Panel will not normally allow a bid to lapse in these circumstances unless the matter would be of sufficient importance such that the Panel would permit the offeror to invoke a condition to lapse the bid as per Rule 13.4(a), whether or not this was included as a specific condition to the bid.

Q7: Do you agree with the proposed amendment to the Note on Rule 2.7 as set out above and to the proposed consequential amendments?

30. We agree.

Q8: Do you agree that Rule 12.2 should be amended as proposed?

31. For the purpose of market and shareholder clarity we believe the Code Committee should consider whether a lapsed bidder, who has received a non-clearance decision, be required itself to put out a Rule 2.8 announcement or whether the competition authority's non-clearance decision announcement will always be sufficiently clear such that the market will know that the lapsed bidder is ruled offside for six months.

Q9: Do you agree with the proposed amendment to Rule 31.3?

32. We agree with the clarifications.

Q10: Do you agree that Rule 25.3(a)(v) should be amended as proposed?

33. We agree.

Q11: Do you agree that Rule 27.1 should be amended as proposed?

34. We agree.

Q12: Do you agree that Note 6 on Rule 9.1 should be amended as proposed?

35. We agree with the proposed amendment but believe that the Panel may **also** be concerned in such circumstances that the vendor is acting in concert with the purchaser. We therefore believe the third sentence in Note 6 should instead read:

    'The Panel will be concerned to see whether in such circumstances the vendor **is acting in concert with the purchaser and/or** has effectively allowed the purchaser...'

Q13: Do you agree that Rule 36 should be amended as proposed?

36. We agree.

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