26 July 2010

Our ref: ICAEW Rep 69/10

Your ref:

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

Dear Sir

PCP 2010/2 CONSULTATION ON REVIEW OF CERTAIN ASPECTS OF THE REGULATION OF TAKEOVER BIDS

ICAEW is pleased to respond to your request for comments on PCP 2010/2 - *Review of certain aspects of the regulation of takeover bids*.

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

Yours sincerely

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ICAEW REPRESENTATION

Memorandum of comment submitted on 26 July 2010 by ICAEW, in response to The Panel on Takeovers and Mergers' consultation paper PCP 2010/2 – *Review of certain aspects of the regulation of takeover bids* published in June 2010

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INTRODUCTION

1. ICAEW welcomes the opportunity to comment on the consultation paper *PCP 2010/2 Review of certain aspects of the regulation of takeover bids* published by The Takeover Panel.

WHO WE ARE

2. 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, we provide leadership and practical support to over 134,000 members in more than 160 countries, working with governments, regulators and industry in order to ensure the highest standards are maintained. We are 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. We ensure these skills are constantly developed, recognised and valued.

MAJOR POINTS

Support for the initiative

4. Given the nature and significance of the issues that have been raised in the current PCP, we are supportive of the approach taken by The Panel on Takeovers and Mergers ('the Panel') in providing a forum in which suggestions for a possible change can be debated.

5. We accept that there are some specific issues which merit examination in respect of UK corporate takeover transactions. However, we believe that these issues are not limited to The Takeover Code ('the Code') or to matters regulated by the Panel, but extend more broadly to company law, corporate governance and employment rules and regulations and therefore there are other bodies and stakeholders that play a part in the corporate takeovers landscape who will need to be consulted (and their regimes co-ordinated) if there were to be any major policy shift in the Code.

6. Notwithstanding the speficic issues noted above, we believe that the current system in place that is overseen by the Panel is fundamentally robust and that the Code should continue to deal with matters that it has been designed to address, as set out in the Introduction section of the Code, without the need for any major change. Furthermore, we are of the view that the Code should not be used as a tool to deal with matters that may be the responsibility of the government or other regulatory bodies.

7. We set out below our responses to the specific questions raised in the PCP.

RESPONSES TO SPECIFIC QUESTIONS

Q1: What are your views on raising the minimum acceptance condition threshold for voluntary offers above the current level of '50% plus one' of the voting rights of the offeree company?

8. We do not believe that the minimum acceptance condition threshold for voluntary offers should be raised. The current level of '50% plus one' is in line with the general principle that the views of the simple majority should (on most issues) prevail which is consistent with current UK company law. Further, any increase in the acceptance threshold would run counter to the reality in the majority of Code companies in which, due to the spread of shareholder ownership, effective control can in fact be achieved at much lower levels than 50%.

Q2: What are your views on raising the acceptance condition threshold for mandatory offers above the current level of "50% plus one" of the voting rights of the offeree company?

9. Our view set out for Q1 equally applies to mandatory offers.

Q3: If you believe that an increase in the acceptance condition thresholds for voluntary and/or mandatory offers would be desirable, at what level do you believe they should be set and why?

10. As set in our responses to Q1 and Q2, we are not in favour of the acceptance condition thresholds being increased.

Q4: What are your views on the consequences of raising the acceptance condition thresholds?

11. Consistent with our reponse to Q1, we are of the view that raising the acceptance condition threshold is against the basic democratic right of a shareholder. Furthermore, if there is to be an increase in the acceptance condition threshold then there should be an equivalent change to company law. We believe that such a change to company law would not only be impractical and inappropriate but would also be against the 'simple majority wins' principle.

Q5: What are your views on the suggestion that shares acquired during the course of an offer period should be "disenfranchised"?

12. We are not in favour of the disenfranchisement of shares acquired during the course of an offer period. It is part of the fundamental property rights of a shareholder that they should be able to vote their shares; disenfranchising shares is, in our view, against the spirit of the 'one share one vote' principle.

13. In addition, disenfranchisement of shares acquired during the course of an offer period would potentially restrict a white knight or another potential offeror from entering the fray which, in our view, is unlikely to be in the best interests of the offeree company's shareholders. This is because often a competing offeror may want to stake-build as part of their bid strategy to prevent the first offeror from succeeding in their offer. Disenfranchisement of shares may therefore frustrate a competing offer.

14. Furthermore, disenfranchisement of shares will also make the enforcement of the disclosure regime more complicated as the denominator to be used to calculate one's interest in securities could potentially change on a frequent basis as trades go through during an offer period. We are of the view that the implications of disenfranchisement should be considered carefully before making any such amendments to the Code.

Q6: If you are in favour of "disenfranchisement", what are your views on how such a proposal should be implemented? In particular, what are your views on the various consequential issues identified in section 3 of the PCP?

15. We are not in favour of disenfranchisement, as stated above.

Q7: What are your views on the suggestion that shares in a company should not qualify for voting rights until they have been held by a shareholder for a defined period of time and regardless of whether the company is in an offer period?

16. In our view, there are other mechanisms, for example the taxation regime, which can be used to shape shareholder behaviour to promote longer term ownership of shares if this were to be regarded as a matter of economic principle as a desirable thing to achieve in the UK. We believe that restricting voting rights for a defined period of time regardless of whether the company is in an offer period is against the 'one share one vote' principle and we are therefore not in favour of such restrictions being imposed and we do not think the scope of the Code should be extended to address this.

17. Furthermore, there may be other regulatory issues that would need to be considered if such restrictions were to be introduced. For example, whether shares with such restrictions would be suitable for listing would need to be considered along with the longer term implications for companies and their shareholders.

Q8: What are your views on the suggestion that the threshold trigger at which independent market participants become subject to the Code's disclosure regime, currently 1%, might be lowered to 0.5%?

18. We note that the recent amendments to the Code's disclosure regime took effect on 19 April 2010 and resulted in an increase in transparency in relation to the positions of, and dealings by, persons involved in takeover offers. We further note that PCP 2005/1 looked into whether the disclosure obligation should arise at the 1% level and, as stated in the Response Statement 2005/2 issued on 5 August 2005, the Code Committee concluded that the disclosure obligation should continue to arise at the 1% threshold. In light of the recent changes to the disclosure requirements and in light of the previous consultation carried out on this matter, we are of the view that the effectiveness of the new disclosure regime should be allowed to be tested for some time before further changes are proposed to the disclosure requirements.

19. We are also of the view that, if a cost benefit analysis was to be conducted, the potential benefit due to the increased transparency resulting from lowering the threshold is likely to be outweighed by the additional costs of compliance (and monitoring by the Panel) as well as the likely overflow of information in the market as a result of the increased number of disclosures.

Q9: What are your views on the suggestion that there should be additional transparency in relation to offer acceptance decisions and of voting decisions in relation to schemes of arrangement? If you are in favour of this suggestion, please explain your reasons and how you think such additional transparency should be achieved?

20. We are of the view that shareholders should not be required to disclose their acceptance/voting decisions. Furthermore, we do not believe that the Panel is the right platform to be used to monitor the behaviour of institutional or other shareholders.

21. However, we recognise that in bid situations the behaviour of certain shareholders (institutional, high-profile investors or large shareholders) may have a significant influence on the decision-making of other shareholders and can sometimes determine the ultimate outcome of a bid.

22. For example, a large shareholder may make statements in the the media to indicate its likely decision with regards to an offer without formally committing to act in a particular way (either through a letter of intent or an irrevocable undertaking). If, subsequently, the large shareholder acts contrary to what other shareholders were initially led to believe then, arguably, the large shareholder's statements may have created uncertainty and may have been misleading. We are of the view that in such a situation, if a shareholder has informally indicated their likely voting decision then the shareholder should be required to clarify their intention by a regulatory announcement, as stipulated by the Code. This would not prevent such a shareholder from subsequently altering its position and updating the market accordingly.

Q10: What are your views on the suggestion that the application of the Code's disclosure regime to situations where the rights attaching to shares have been "split up" might be clarified?

23. We understand that there may be circumstances where certain of the decisions regarding dealing, voting and offer acceptances have been delegated by the beneficial owner to a fund manager. In our view, such delegation is a matter between the beneficial shareholder and the party to which such decision-making rights have been delegated and should not be a matter that requires disclosure under the Code. However, as noted in the PCP, the number of cases where there is "split up" of decisions is increasing. If the Panel feels that this is a matter that merits disclosure and would enhance the regulation of takeover matters then this should be looked into further.

Q11: What are your views on the suggestion that the same requirements as to the disclosure of financial information on an offeror, the financing of the offer, and information on quantified effects statements should apply regardless of whether:

(a) the consideration being offered is cash or securities;

(b) the offer could result in minority shareholders remaining in the offeree company; or

(c) the offer is hostile or recommended, or whether a competitive situation has arisen?

24. We believe that the current treatment under the Code in respect of the disclosure of financial information on an offeror, the financing of the offer and information on quantified effects statements should continue to apply and therefore the same disclosure requirements in the situations outlined above are not necessary.

Q12: What are your views on:

(a) disclosures made by offerors of their intentions in relation to the offeree companies under Rule 24.1; and

(b) the views of the boards of offeree companies on offerors' intentions given under Rule 25.1?

If you consider that greater detail is required, how do you consider that this would be best achieved?

25. Rule 24.1 sets out the disclosures that an offeror is required to make, *inter alia*, regarding its intentions in relation to an offeree company. However, we are of the view that offer documents normally disclose no more than the bare minimum amount of information to ensure compliance with the letter of the Code rather than its spirit. As a result, such disclosure does not always give shareholders the full picture of an offeror's strategic plans going forward to enable them to make an informed decision. We believe that a Practice Statement in this regard providing guidance as to the nature and level of detail that offerors should include in an offer document would be an appropriate way of addressing this issue rather than requiring an amendment to the rule itself.

26. Rule 25.1 requires the views of the board of an offeree company on an offer to its shareholders. The views of the board of an offeree company are dependent on how much

information they are privy to with regards to an offeror's intentions in respect of the offeree company. We therefore believe that a Practice Statement addressing Rule 24.1 and Rule 25.1, and requiring more detail regarding these matters to be provided in offer documents, would be an appropriate way of dealing with this matter rather than requiring any amendments to these specific rules.

Q13: What are your views on the matters to which the board of the offeree company should have regard in deciding whether or not to recommend acceptance of an offer?

27. We do not believe that the Code should stipulate the considerations that the board of an offeree company should have regard to in deciding whether or not to recommend acceptance of an offer. This is a matter which should be a matter of jurisprudence and it is already regulated by company law (case law and statute). Accordingly, directors should take into account their fiduciary duties as set out in company law including, specifically, the matters set out under section 172 of the Companies Act 2006.

Q14: What are your views on the suggestion that there should be a requirement for independent advice on an offer to be given to offeree company shareholders separately from the advice required to be given to the board of the offeree company?

28. We think that there are going to be practical difficulties in persuading financial advisers to provide advice to offeree company shareholders (whilst maintaining appropriate standards), as noted in paragraph 6.11 of the PCP. Even if a financial adviser is prepared to give such advice to offeree company shareholders, we are not convinced that the work undertaken would be significantly different from an independent adviser that is required to provide advice to the board of the offeree company and therefore the benefits are likely to be outweighed by the costs of such an additional professional advisory cost. We are therefore not in favour of requiring independent advice for offeree company shareholders and believe that the current approach should continue to apply.

Q15: What are your views on the suggestion that the board of an offeree company should be restricted from entering into fee arrangements with advisers which are dependent on the successful completion of the offer?

29. We are of the view that success fees are not significant enough to compensate for an adviser's reputational risk and therefore we do not think that fee arrangements which are dependent on the successful completion of the offer should be restricted.

Q16: What are your views on the suggestion that the fees incurred in relation to an offer should be required to be publicly disclosed?

30. Our view in relation to this matter is that this is likely to lead to increased transparency and may be perceived positively by shareholders of offeree companies.

Q17: If you are in favour of the disclosure of fees, how do you think that any provision should operate? For example:

(a) to which fees (and other costs) should any provision apply and on what basis?

(b) at what point(s) of the transaction should any disclosure be made?

31. In our opinion, the aggregate fee to be incurred by the offeree company should be disclosed as well as a separate disclosure highlighting the Rule 3 adviser fee. Such disclosure should also disclose any success fee elements payable. However, we are of the view that such disclosure should not result in sensitive information about offer tactics being revealed. For example, advisers could be required to disclose the range of fee that may be payable taking into account any ratchet mechanism without being required to provide the specific terms of the ratchet mechanism to avoid disclosing any sensitive information that may compromise the offeree company's bid tactics.

32. We believe that such disclosure should be first disclosed at the time of the Rule 2.5 announcement.

Q18: What are your views on the suggestion that shareholders in offeror companies should be afforded similar protections to those afforded by the Code to offeree company shareholders?

33. We do not consider that offeror company shareholders should be afforded protections under the Code unless the relevant circumstances, as set out in Rule 3.2 are applicable. Therefore, in our view, the current remit of the Code to protect the interests of shareholders of the offeree company should not be extended to shareholders of the offeror companies.

34. In particular, where an offeror is an overseas company, it would be impractical to expect the Panel to be able to enforce the Code on such overseas companies. This extra-territorial reach of the Code would not be welcome and may lead to unhelpful counter-measures by overseas regulators – regulatory reach warfare – which would be unwelcome. Furthermore, the Code requirements may not be consistent with the local regulatory requirements.

35. It would be undesirable for overseas offerors to be treated differently from UK offerors. On this basis, we believe that it would not be feasible for protections of the Code to be offered to offeror company shareholders.

Q19: If you consider that offeror company shareholders should be afforded protections:

(a) to which offeror companies should such protections apply and in what circumstances?

(b) what form should such protections take?

(c) by whom should such protections be afforded (for example, the Panel, the FSA, the Government or another regulatory body)?

36. We do not believe that offeror company shareholders should be afforded protections under the Code unless, as mentioned above, Rule 3.2 is applicable.

Q20: What are your views on the suggested amendments to the 'put up or shut up' regime? In particular:

(a) what are your views on the suggestion that 'put up or shut up' deadlines might be standardised, applied automatically and/or shortened?

(b) what are your views on the suggestion that a 'private' 'put up or shut up' regime might be introduced?

37. We do not believe that 'put up or shut up' deadlines should be standardised, applied automatically or shortened. This is because we think that each situation needs to be considered in light of its individual circumstances and therefore the Panel's current regime of setting 'put up or shut up' deadlines based on the merits of each case should continue to apply.

38. Our view in respect of a private put up or shut up is that one can see some benefit of such regime being introduced. In most situations, discussions between an offeror and offeree commence before an offer period starts. As certain provisions of the Code, for example Rule 21.1, start applying as soon as an approach has been received by the offeree company it could be argued that there may be situations where the offeree company could be put under 'siege' at that point due to the restrictions imposed on it. To enable an offeree company to end such a siege, it could be contended that it should be able to apply for a private put up or shut up deadline.

39. As noted in the PCP, an offeree board company can always resolve such a siege situation by publicly disclosing the potential offeror's existence and then seeking a put up or shut up deadline. However, arguably, this may not always be in an offeree company's interests as it

may have to put itself into an offer period in order to seek such a deadline, thus unnecessarily putting itself in play which may be seen as a rather disproportionate way of allowing an offeree company out of an offer period.

40. In light of the above, we consider that the merits of introducing a private put up or shut up regime may have to be publicly consulted before making any amendments to current practice. Furthermore, consideration should also be given to how the situation would be dealt with if the existence of a private put up or shut up is leaked and becomes public.

Q21: What are your views on possible offer announcements that include the possible terms on which an offer might be made and/or that includes pre-conditions to the making of an offer?

41. In our view, possible offer announcements with possible terms including pre-conditions should continue to be allowed as long as a prominent warning to the effect that the announcement does not amount to a firm intention to make an offer is included. The purpose of the Code is not to restrict transactions from taking place and there may be commercial aspects to a transaction which may necessitate a potential offeror stating such pre-conditions to ensure that the market is aware of the potential hurdles before it would consider making a firm announcement.

Q22: What are your views on the deadline for the publication of the offer document and the suggestion that the current 28 day period between the announcement of a firm intention to make an offer and the publication of the offer document might be reduced?

42. We are of the view that, in practice, offerors do not normally utilise the full 28 day period allowed to post an offer document. However, as set out in the PCP, there may be situations where an offeror may be unable to produce an offer document within a shorter timeframe. We would recommend a more detailed analysis (supported by data) to obtain a better understanding of the extent to which the 28 day period is used, before any decisions to alter the rule are made. If there is evidence to suggest that the posting time can be reduced without impacting the quality and level of detail that offerors should be including in an offer document, then this should be looked into further.

Q23: What are your views on the suggestion that the Panel should have the ability unilaterally to foreshorten the timetable for subsequent competing offers?

43. We do not believe that the Panel should have the ability to unilaterally foreshorten the timetable for subsequent competing offers. We are of the view that each competing offeror should be allowed the same timeframe in which to make an offer.

Q24: What are your views on the Panel's approach to inducement fees? In particular:

(a) do you consider that inducement fees should be prohibited?

(b) if you consider that inducement fees should continue to be permitted:

(i) do you regard the *de minimis* nature of inducement fees (and the Panel's approach to what is *de minimis*) as a sufficient safeguard?

(ii) do you consider that any further restrictions should be imposed on inducement fees by the Panel (for example, in relation to the timing of payment or the triggers for payment)?

(iii) what are your views on the suggestion that the Panel should cease to require confirmations from the offeree company board and its financial adviser that they each believe the inducement fee to be in the best interests of shareholders?

44. We do not believe that inducement fees should be prohibited.

45. We regard the current *de minimis* level for inducement fees to be a sufficient safeguard. We also note that many other regimes/ jurisdictions do not have in place such caps and indeed the

practice is to enter into higher break fees (eg, USA: between 3% and 6%) which we do not believe has had any adverse impact on the competitive landscape for bids there.

46. We are of the view that it is a matter for the offeror and offeree to decide upon the contractual terms of inducement fee arrangements and therefore do not consider that it is for the Panel to impose any further restrictions in this regard.

47. There is an argument that confirmations provided to the Panel from the offeree company board and its financial adviser regarding inducement fee arrangements are becoming a box-ticking exercise and have limited value. Notwithstanding this limitation, we are of the view that if an offeree company decides to enter into more than one inducement fee arrangement then the significance of such a confirmation increases and requiring such a confirmation will ensure that the board of the offeree company and the financial adviser 'focus their minds' before entering into such arrangements. As such, in our view, the confirmations currently required by the Panel should continue to be applicable.

Q25: What approach should the Panel take to deal protection measures? In particular, do you consider that any specific deal protection measures should be either prohibited or otherwise restricted? Please explain reasons for your views.

48. We are of the view that the offeror and offeree should be able to negotiate deal protection arrangements between themselves without Panel involvement. We therefore do not consider that any specific deal protections should be prohibited or restricted and that offeree company directors should consider their fiduciary duties under company law when entering into such arrangements.

Q26: What are your views on the suggestion that implementation agreements and other agreements containing deal protection measures should be required to be put on display earlier than at present?

49. In our view, such agreements should be required to be put on display earlier than at present and doing so at the time of the 2.5 announcement would be more appropriate.

Q27: What are your views on "fiduciary outs" in the context of inducement fee arrangements?

50. We do not believe that 'fiduciary outs' are something that the Code should be stipulating. In our view, and as noted in paragraph 9.22 of the PCP, in practice it is too difficult for the board of the offeree company to be able to rely on fiduciary outs. Furthermore, fiduciary outs may be regarded by offerors as having the effect of invalidating the commercial reasons for entering into such an arrangement.

Q28: What are your views on the ability of deal protection measures to frustrate a possible competing offer and on whether linking deal protection measures to the payment of an inducement fee may cure any such potential frustration?

51. We are of the view that given the *de minimis* nature of inducement fee arrangements, deal protection measures do not frustrate a possible competing offer.

52. In respect of linking deal protection measures to the payment of an inducement fee, we are of the view that the specific terms of such arrangements should be left to the offeror and offeree to decide and should not be determined by the Panel.

Q29: What are your views on the suggestion that provisions similar to those previously set out in the Rules Governing Substantial Acquisitions of Shares should be re-introduced?

53. We understand that the Code applies to situations where control of an offeree company is being obtained or is being consolidated. Therefore, our view is that stake-building below the control threshold is not something that should be regulated by the Code. Hence, we are not in favour of the re-introduction of such rules. We also have concerns that, given the current statutory powers of the Panel, such an amendment would be *ultra vires.*