



**PCP4 Issued on 5 September 2001**

**THE PANEL ON TAKEOVERS AND MERGERS**

**CONSULTATION PAPER ISSUED BY  
THE CODE COMMITTEE OF THE PANEL**

**DISCLOSURE OF SIDE AGREEMENTS  
RELATING TO OFFER PRE-CONDITIONS AND  
CONDITIONS**

**REVISION PROPOSALS RELATING  
TO RULES 2.5, 24.2 AND 26  
OF THE TAKEOVER CODE**

Before it introduces or amends any Rules of the Takeover Code or the Rules Governing the Substantial Acquisitions of Shares, the Code Committee of the Takeover Panel is required under its consultation procedures to publish the proposed Rules and amendments for public consultation and to consider responses arising from the public consultation process.

The Code Committee is therefore inviting comments on this Consultation Paper. Comments should reach the Code Committee by **5 October 2001**.

Comments may be sent by email to:

[consultation@disclosure.org.uk](mailto:consultation@disclosure.org.uk)

Alternatively, please send comments in writing to:

The Secretary to the Code Committee  
The Panel on Takeovers and Mergers  
P.O. Box No. 226  
The Stock Exchange Building  
London  
EC2P 2JX

Telephone: 020 7382 9026

Fax: 020 7638 1554

It is the Code Committee's policy to make all responses to formal consultation available for public inspection unless the respondent requests otherwise.

## **1. Introduction**

1.1 The Code Committee has been considering whether the Code should require the public disclosure of any agreements or arrangements to which an offeror is party which relate to (a) the circumstances in which it may or may not invoke or seek to invoke an acceptance condition to its offer (or indeed any other condition or pre-condition to its offer), or (b) the consequences of it doing so. There is currently no Rule in the Code which relates to this matter and consequently there is no uniform practice in this area. The Code Committee has concluded that the Code should be amended to require the public disclosure of such agreements or arrangements and

sets out below the text of the proposed amendments and the reasons for its conclusions.

- 1.2 For the purposes of this paper, an "acceptance condition" means any condition to an offer which requires the offeror to have received valid acceptances of the offer (or of any other offer made by the offeror) in excess of a stipulated threshold.

## **2. Text of the Proposed Amendments**

- 2.1 It is proposed that a new Rule 2.5(b)(vi) is introduced as follows:

*"(b)(vi) details of any agreements or arrangements to which the offeror is party which relate to the circumstances in which it may or may not invoke or seek to invoke a pre-condition or a condition to its offer and the consequences of it doing so, including details of any break fees payable as a result;"*

It is proposed that the existing Rules 2.5(b)(vi) and (vii) are re-numbered accordingly. As discussed below, if it is concluded that side agreements relating to acceptance conditions alone should be disclosed, then the words "a pre-condition or a" in line 3 should be replaced by "an acceptance".

- 2.2 It is proposed that a new Rule 24.2(d)(vii) is introduced in the same form as the proposed new Rule 2.5(b)(vi) save that the words "a pre-condition or" will not be included in line 3 of Rule 24.2(d)(vii). It is proposed that the existing Rules 24.2(d)(vii) and (viii) are re-numbered accordingly.

- 2.3 It is proposed that a new Rule 26(n) is introduced as follows:

*"(n) documents relating to any agreements or arrangements disclosed in the offer document pursuant to Rule 24.2(d)(vii)."*

Consequential changes will be required to Rules 26(1) and (m).

### **3. Reasons for the Proposed Amendments**

#### *3.1 Acceptance conditions*

3.1.1 Given the significance of conditions in evaluating the likely success of an offer, the Code not only requires that they are set out in the offer document, but also that they are included in the offer announcement made under Rule 2.5 of the Code. The purpose of this requirement is to enable both offeree shareholders and the market as a whole to have at their disposal at the earliest possible stage the information necessary to evaluate, on the one hand, the factors which could cause an offer to fail and the risk of the offeror seeking to lapse its offer (subject always to the provisions of Note 2 on Rule 13) and, on the other hand, the likelihood of an offeror declaring an offer unconditional as to acceptances once it has satisfied the Rule 10 acceptance threshold.

3.1.2 The Code Committee has, however, been made aware of certain recent cases in which an offeror has entered into a side agreement which related directly to the circumstances in which it may or may not invoke or seek to invoke an acceptance condition to its offer and the consequences of it doing so. Examples include, in the context of a standard 90% waivable down to 50% acceptance condition: (i) an agreement by an offeror in a leveraged buy-out not to waive down the acceptance condition to a level below 75% acceptances, and not to waive down the same condition below 90% acceptances without the prior written consent of the lending banks; and (ii) an agreement by an offeror not to lapse its offer pursuant to the

acceptance condition prior to day 60 (and, if it did so, to pay the offeree a break fee). In certain cases, details of these agreements have been disclosed in the offer document (sometimes on a partial basis only) but not in the offer announcement and in others they were not disclosed in either the offer document or the offer announcement.

3.1.3 The Code Committee believes that the existence and details of any agreements or arrangements of this nature are material information both for offeree shareholders and for the market. Furthermore, the Code Committee is concerned that, absent such information being made available, a person reviewing an acceptance condition to an offer is not able to make a truly informed assessment of the risk of the offer lapsing or indeed succeeding. General Principle 4 of the Code requires that:

*"Shareholders must be given sufficient information and advice to enable them to reach a properly informed decision and must have sufficient time to do so. No relevant information should be withheld from them."*

Likewise, the Code Committee is concerned that, absent such information being made available, an incomplete picture may be presented. General Principle 6 requires that:

*"All parties to an offer must use every endeavour to prevent the creation of a false market in the securities of an offeror or the offeree company. Parties involved in offers must take care that statements are not made which may mislead shareholders or the market."*

## 3.2 *Other conditions*

3.2.1 The Code Committee also understands that similar side agreements have been

entered into in respect of conditions to an offer other than an acceptance condition. Examples include, in the context of regulatory conditions: (i) undertakings by an offeror to an offeree to sell specified businesses in the event of this being required either in order to avoid a reference to a higher competition authority or in order for the bid to be cleared; and (ii) an agreement by an offeror to pay the offeree a break fee in the event that it lapsed its offer pursuant to a particular regulatory condition.

3.2.2 The Code Committee believes that it is logically consistent to say that, if the Code is to be amended to require the disclosure of side agreements relating to acceptance conditions, it should also be amended to require the disclosure of side agreements relating to other conditions, including regulatory conditions (and also any term to an offer included pursuant to either Rule 12.1(a) or (b) of the Code), on the basis that such information is equally material to offeree shareholders and the market. The Code Committee also believes that the new disclosure requirements should apply to side agreements or arrangements to pre-conditions to an offer. This is on the basis that details of any such agreement or arrangement is relevant information for parties dealing in offeror and offeree securities in the market while the offer is subject to the pre-condition in question, albeit that at this time offeree shareholders are not required or able to make an acceptance decision.

3.2.3 It is not intended that the proposed amendments should require the public disclosure of a disclosure letter entered into between an offeror and an offeree where one or more of the conditions to the offer contains an explicit carve out for information disclosed in writing by the offeree or its advisers to the offeror or its advisers. A disclosure letter is a standard and legitimate mechanism, well understood by investors, for ensuring that an offeror is not able to invoke a condition where, at the time that the offer is announced, it has knowledge of matters which would otherwise give it that right. Furthermore, the Code Committee believes that it would be inappropriate to require that the terms of such a letter, which may contain commercially sensitive and confidential information, be publicly disclosed and put

on display.

### 3.3 *Advantages and disadvantages*

3.3.1 The potential disadvantages with the proposed requirement for the public disclosure of side agreements to offer pre-conditions and conditions are considered to be as follows:

- (i) is a change to the Code really necessary? Offerees and their advisers are free to negotiate such agreements and the need for their public disclosure;
- (ii) it is often the case that, because the public documents indicate no constraints on the invocation of the conditions, the actual position is in fact more favourable than what is disclosed and so there are no downside concerns for offeree shareholders or the market;
- (iii) a requirement for such disclosure may weaken the negotiating position of the offeree and its advisers. This may be particularly relevant where, for example, an offeree is seeking commitments from an offeror (e.g. to sell specified businesses) in the event of it being notified that regulatory clearance will only be granted subject to certain conditions.

3.3.2 The Code Committee is of the opinion that the following points can be made in response to these concerns:

- (i) although offerees and their advisers are free to negotiate the public disclosure of such agreements, this does not always happen in practice. The Code Committee believes that the Code should impose a consistent policy in this area;

- (ii) although it will often be the case that any negotiated side agreement will only represent "upside" for shareholders (e.g. the offeror agrees with the offeree not to invoke the acceptance condition if it has received, say, at least 75% acceptances notwithstanding the publicly stated 90% acceptance condition waivable down to 50%), there may be other types of agreement reached which may represent "downside" for shareholders (e.g. an offeror and offeree agree a materiality threshold for the purposes of an environmental audit condition which is lower than that which the market would normally expect);
  
- (iii) the Code Committee does not believe that an offeree's negotiating position would be materially weakened by the proposed amendments. At worst, it may lead to a more fervent negotiation of the offer conditions. If, however, it was considered that, in the context of regulatory pre-conditions and conditions, an offeree's negotiating position would be unduly compromised due to the fact that the relevant regulatory authority would be made aware of the concessions which an offeror may be prepared to make in order to obtain clearance, it would be possible for the Executive to grant dispensations in the context of regulatory pre-conditions and conditions only. The Executive would only grant a dispensation where the offeree and its advisers confirmed to the Executive in writing that they believed that it was in shareholders' interests that the side agreement in question was not disclosed as to do so would result in the offer not being made or in an offer being made on less beneficial terms.

3.3.3 In summary, the Code Committee is of the opinion that it is not acceptable that agreements which are essential to a proper understanding of the offer pre-conditions and conditions should remain undisclosed (or should be disclosed on a partial basis



only), particularly given that the Executive's ability to require the enforcement of such agreements is dependent upon their terms being publicly disclosed. In accordance with normal Code principles, where a party to an offer makes a public statement of its intended actions in relation to the offer, the Executive will hold the party to that statement. Where, however, an arrangement remains a private agreement to the parties to an offer, the Executive is not able to intervene.

3.3.4 Accordingly, the Code Committee believes that the Code should be amended as set out in paragraph 2 above – that is to say, full details of any agreements or arrangements to which an offeror is party which relate to the circumstances in which it may or may not invoke or seek to invoke any pre-condition or condition to its offer and the consequences of it doing so, including details of any break fees payable as a result, should be included in both the announcement of the firm intention to make an offer made under Rule 2.5 of the Code and, in relation to conditions only, the offer document. In addition, a copy of all documents relating to any such agreements or arrangements should be put on display under Rule 26.

#### **4. The Effect of the Proposed Amendments**

4.1 If side agreements or arrangements of the kind referred to above are entered into and are publicly disclosed in the manner proposed, then, as stated above, the offer must be conducted, and the parties will be required to behave, in a manner which is consistent with what has been publicly stated.

4.2 It should be noted that the proposed amendments do not in any way affect the Panel's position on the ability of an offeror to lapse an offer, which is set out in Note 2 on Rule 13.

4.3 The Code Committee believes that the cost implications of this amendment for

offerors and offerees will be minimal.

## **5. Questions**

- (1) Do you agree that the Code should be amended to require the public disclosure of any agreements or arrangements to which an offeror is party which relate to the circumstances in which it may or may not invoke or seek to invoke an acceptance condition to its offer and the consequences of it doing so?**
  
- (2) If you agree with (1), do you also agree that the Code should be amended to require the public disclosure of any agreements or arrangements to which an offeror is party which relate to the circumstances in which it may or may not invoke or seek to invoke any other condition to its offer and the consequences of it doing so?**
  
- (3) If you agree with (2), do you also agree that the Code should be amended to require the public disclosure of any agreements or arrangements to which an offeror is party which relate to the circumstances in which it may or may not invoke or seek to invoke any pre-condition to its offer and the consequences of it doing so?**
  
- (4) If you have a concern with (2) and (3) in the context of regulatory pre-conditions and conditions, do you agree that this can be satisfactorily addressed by the Panel being permitted to grant dispensations in the context of such pre-conditions and conditions where the offeree and its advisers confirm to the Panel in writing that they believe it to be in shareholders' interests for a particular side agreement not to be disclosed as to do so would result in the offer not being made or in an offer being made on less beneficial terms?**