27 May 2011

Our ref: ICAEW Rep 55/11

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

By email: supportgroup@thetakeoverpanel.org.uk

Dear sirs

PCP 2011/1 REVIEW OF CERTAIN ASPECTS OF THE REGULATION OF TAKEOVER BIDS PROPOSED AMENDMENTS TO THE TAKEOVER CODE

ICAEW is pleased to respond to your request for comments on PCP 2011/1 Review of certain aspects of the regulation of takeover bids, Proposed amendments to the Takeover Code.

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

Yours faithfully

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ICAEW REPRESENTATION

PCP 2011/1 REVIEW OF CERTAIN ASPECTS OF THE REGULATION OF TAKEOVER BIDS, PROPOSED AMENDMENTS TO THE TAKEOVER CODE

Memorandum of comment submitted in May 2011 by ICAEW, in response to the Code Committee of the Takeover Panel's consultation on *Proposed amendments to the Takeover Code* issued in March 2011

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INTRODUCTION

1. ICAEW welcomes the opportunity to comment on *PCP 2011/1, Proposed amendments to the Takeover Code* published by the Code Committee of the Takeover Panel in March 2011.

WHO WE ARE

2. ICAEW is a world-leading professional accountancy body. We operate under a Royal Charter which obliges us to work in the public interest. ICAEW's regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the UK Financial Reporting Council. We provide leadership and practical support to over 136,000 member chartered accountants in more than 160 countries, working with governments, regulators and industry in order to ensure that the highest standards are maintained.

3. ICAEW members operate across a wide range of areas in business, practice and the public sector. They provide financial expertise and guidance based on the highest professional, technical and ethical standards. They are trained to provide clarity and apply rigour, and so help create long-term sustainable economic value.

4. ICAEW's Corporate Finance Faculty is a network of some 5,000 corporate finance professionals. The faculty regularly responds to consultations from government, listing authorities and regulators in the UK and overseas. 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

5. We agree with a number of the changes proposed in PCP 2011/1. We welcome the provisions intending to provide greater recognition of the interests of employees of the offeree and simultaneously believe that specific guidance from the Panel would be very helpful for dealing with employee issues.

6. We disagree with the following proposed amendments:

- the mandatory naming of bidders;
- the inflexible new mandatory 'put up or shut up' regime; and
- the prohibition of inducement fees.

7. We consider that these proposals, together with certain excessive information requirements (such as new Rule 24.16) will have a cumulative effect of deterring bidders or, at least, making them more vulnerable to financial and reputational risk associated with failed bids, without necessarily protecting target boards and the interests of target shareholders.

8. We would strongly urge the Panel to give target boards the option of naming a potential bidder. The benefits of this measure would be to achieve more empowerment of target boards (one of the Panel's aims) and to help prevent a reduction in the volume of bids at a time when M&A activity is already severely depressed. Moreover, the 28-day time limit may induce a higher degree of risk into takeovers with less time available for due diligence and for arranging the optimal financing needs and capital structures.

RESPONSES TO SPECIFIC QUESTIONS

INCREASING THE PROTECTION FOR OFFEREE COMPANIES AGAINST PROTRACTED "VIRTUAL" BID PERIODS

Q1 Do you have any comments on the proposed new Rule 2.4 and the proposed new Note 3 on Rule 2.2?

9. We strongly disagree with the principle of mandatory naming of a bidder as prescribed in new Rule 2.4 and believe that the anonymity permitted to a white knight provides an unfair advantage compared to other offerors.

10. This measure may be counterproductive to the stated aim of reducing the offeror's tactical advantage. In the experience of our members, there are situations where not naming the bidder is a tactical advantage to the offeree and identifying the bidder could reduce the target board's negotiating ability by giving potential bidders information on other bids.

11. Many of our members who are close to the current sentiment of offerors are concerned that naming of bidders will deter possible offerors, including consortium bidders and sovereign wealth funds as well as those backed by private equity or other financial sponsors. Each of these groups may have serious concerns about being prematurely named, either because they are more conservative and do not wish their strategy to be revealed too early or where there is little appetite for reputation risk. It is hard to see how it would be in the interest of shareholders if deals do not proceed because bona fide potential bidders are reluctant to be disclosed.

12. We are also not persuaded by the argument that simply naming the potential offeror will allow the market to assess the likelihood and quality of a bid or how much the bidder will pay.

13. Finally, in our view, the proposed regime will not remove the risk of offerors 'outing' themselves in that a potential offeror may still be incentivised to leak themselves or others in order to determine the competitive landscape.

14. We would urge the Panel to give target boards the option of naming a potential offeror. The benefits of this measure would be to achieve more empowerment of target boards (one of the Panel's aims) and to help prevent a reduction in the volume of bids in a market when M&A activity is already severely depressed. A reduction in demand for takeovers may also have a dampening effect on valuations which, again, would not be in the interest of target shareholders.

Q2 Do you have any comments on the proposed new Rule 2.6(a)?

15. We have serious concerns with the accelerated timing following a possible offer announcement. We believe it does not provide a realistic time for a buyer's due diligence, for the right form and/or mix of consideration to be determined and for any debt finance to be negotiated. While this will prejudice financial buyers in particular, such a squeezed timeframe will mean that many buyers will be forced to make a possible offer announcement before they are ready and thus may have to terminate their proposal due to being 'timed out'.

16. Moreover, the 28-day time limit may induce a higher degree of risk into takeovers with less time available for due diligence and for arranging the optimal financing needs and capital structures.

17. We also believe that a potential offeror should be able, in certain exceptional circumstances and at the discretion of the Panel, unilaterally to apply for an extension to the deadline otherwise the need for joint application risks giving leverage to the target in a way that unfairly disadvantages a bona fide offeror. If an offeror subsequently walks away then there will be no bid on the table at all for the target shareholders. An example of exceptional circumstances might be if a target changes its mind to apply for an extension.

Q3 Do you have any comments on the possible alternative approach to the identification of potential offerors?

18. We consider that the alternative, private approach to identifying potential offerors is preferable to the mandatory naming of bidders. This would avoid the possible consequences outlined in our response to Q1.

Q4 Do you have any comments on the proposed new Rules 2.6(b), (d) and (e) and Rule 2.3(d)?

19. We note that new Rules 2.6(b), (d) and (e) will lead to multiple 'put up or shut up' deadlines running for different bidders and observe that this will create a messy, confusing situation for the market.

Q5 Do you have any comments on the proposed new Note 2 on Rule 2.6?

20. As mentioned in our response to Q2, we disagree with the 28-day time limit and believe there should be no difference between public and private bids. We would also point out that the wording of the lead-in to this exception to Rule 2.6 differs unnecessarily to that in proposed new Note 2 on Rule 21.2 (Q11).

Q6 Do you have any comments on the proposed new Rule 2.6(c) and Note 1 on Rule 2.6?

21. In Note 1 to Rule 2.6, the Panel's decision on whether or not to grant an extension to the deadline will normally be given "shortly before the time at which the deadline in due to expire". If this is eg Day 25, too much money and time will have been committed. There are so many processes that have to be put in place to make a formal announcement that the offeror must have reasonable notice of whether it is working towards a possible PUSU deadline or has the benefit of an extension.

22. Without sufficient time there is a risk that the offeror may have to work on a dual track process which would be detrimental to target shareholder interests, either because additional wasted costs may adversely impact the offer price or, if the process is tipped too far against the offeror, shareholders risk being deprived of offers.

23. In our view the fact that an offeror can re-enter the process if another offeror makes a Rule 2.5 announcement does not mitigate the impact of a lost bid nor the deal uncertainty created if an extension is not granted.

24. Finally, it would be useful to know what kind of assessment the Panel expects to undertake on the stage of progress of the offeror and offeree on the bid when presented with a request for an extension.

Q7 Do you have any comments on the proposed amendments to Rule 2.8 and to the Note on Rules 35.1 and 35.2?

25. We have no comments.

Q8 Do you have any comments on the proposed framework to be applied in circumstances where, following a requirement to make an offer being triggered under Rule 2.2(c) or (d), a

potential offeror ceases actively to consider making an offer, or on the proposed new Note 4 on Rule 2.2?

26. We have no comments on the proposed framework.

27. We note that certain additional changes which are not the subject of a particular question are characterised as "Minor and consequential amendments". However we are of the view that the proposed wording of new final paragraph to Note 1 on Rule 2.5 is not minor. Furthermore while we agree that neither the total value nor the value of the individual components (eg cash or share element) can be reduced, it should be permissible to vary the mix of the offer (eg to increase the cash element alone).

STRENGTHENING THE POSITION OF THE OFFEREE COMPANY

Q9 Do you have any comments on the proposed new Rule 21.2?

28. We disagree with the general prohibition on offer-related arrangements as set out in new Rule 21.2. This is consistent with our view expressed in ICAEW response to PCP 2010/2. We believe that the measure

- will have a disproportionate effect on smaller businesses;
- could deter any bidder, not just one offering more; and
- will have a significant impact if there are fewer private equity backed bids.

29. In our view, instead of prohibiting such negotiating tools, it would be preferable to require shareholder approval. Furthermore, guidance from the Panel for disclosure of the nature and cost of such arrangements would enhance transparency and understanding of shareholders.

30. We believe there should be more clarity on what distinguishes 'irrevocable commitments' given by directors in para 3.11(d) from 'any commitments' in para 3.12.

31. There is also a lack of clarity as to the position of directors in para 3.12 and the new Rule 21.2(a) that bans, except with the Panel's consent, "any person acting in concert" with the offeror entering an offer-related arrangement with the offeree.

Q10 Do you have any comments on the proposed new Note 1 on Rule 21.2?

32. We disagree with the principle in proposed new Note 1 on Rule 21.2 of allowing inducement fees for one competing offeror (a white knight) and disallowing them for another offeror, including one with a higher bid. We also consider that the dispensations from the general prohibition of inducement fees are overly prescriptive on a matter that is a commercial judgement for directors.

Q11 Do you have any comments on the proposed new Note 2 on Rule 21.2?

33. We generally disagree with principle of, and the carve-outs from, the prohibition of inducement fees. We believe that proposed new Note 2 on Rule 21.2 draws an artificial distinction between public auctions that are announced and those that are not and there should be no distinction between private and public bids.

Q12 Do you have any comments on the proposed new Note 3 on Rule 21.2?

34. As already mentioned, we generally disagree with the carve-outs from the prohibition of inducement fees.

35. In relation to the commentary in para 3.21 on Rule 21.2, although not the subject of a specific question, we also do not consider there are strong reasons for a distinction to be made where a target in financial distress approaches an offeror.

Q13 Do you have any comments on the proposed new Note 4 on Rule 21.2?

36. We have no comments.

Q14 Do you have any comments on the proposed amendments to Appendix 7?

37. We note that target companies incorporated in other EEA jurisdictions, which may be subject to oversight by the Panel in dual jurisdiction cases, may set acceptance conditions at levels other than 90% of the shares to which the offer applies. We suggest that the final sentence in new Note 2 on Section 8 of Appendix 7 is redrafted as follows:

"…with an acceptance condition set <u>at the level required to implement squeeze out</u>."

Q15 Do you have any comments on the proposed new Note 1 on Rule 25.2 or the related amendments?

38. We are uncomfortable with the inclusion of proposed new Note 1 on Rule 25.2 that, in our opinion, addresses in an unsatisfactory manner, an area outside the jurisdiction of the Code; namely, directors' duties. The language used is not necessarily consistent with duties of directors in target companies incorporated in other EEA jurisdictions (which may be subject to regulation under the Code). The last sentence in particular is a negative statement that is potentially confusing and that sets a precedent of matters outside its remit where the Panel provides guidance.

39. As a general point we feel that the Panel is attempting to serve the interests of too many parties – including ones not within its usual jurisdiction by requiring certain disclosures aimed at protecting the interests of the offeror's employees, customers and suppliers (para 6.1(a)(ii)).

INCREASING TRANSPARENCY AND IMPROVING THE QUALITY OF DISCLOSURE

Q16 Do you have any comments on the proposed new Rules 24.16(a) and 25.8?

40. We agree with the overall aim of increasing transparency and improving the quality of disclosure but consider some of the proposals on offeror fees to be excessive. Re new Rule 24.16(a) we do not consider that disclosure of an estimate of the fees and expenses expected to be incurred by the bidder in connection with the offer serves a valid purpose (such as protection of a target's shareholders).

41. In new Rule 25.8, where a split is possible, we consider that this detail could be provided in relation to some of the larger fees under the offer.

Q17 Do you have any comments on the proposed new Note 1 on Rule 24.16?

42. We believe that the proposal may have a disproportionate effect on financial bidders including private equity offerors. We consider that aggregate disclosure of financing fees and expenses would be less onerous and costly for bidders to disclose and would point out that such a level of detail is also consistent with disclosures in an IPO. Fees with success or contingent arrangements should also be described.

Q18 Do you have any comments on the proposed new Rule 24.16(b) and Note 2 on Rule 24.16?

and

Q19 Do you have any comments on the proposed new Rules 24.16(c) and (d)?

43. We consider the proposed approach for cases where fees and expenses exceed the disclosed estimates is unnecessarily complicated.

44. We consider that guidance is needed in the Response Statement as to

- whether the assumptions underlying fee estimates should also be set out;
- the level of materiality the Panel would expect advisers to apply when considering whether disclosure to the Panel of any variation in fees should be made by advisers; and
- the level of variation that would prompt the Panel to require public disclosure.

Q20 Do you have any comments on the proposed deletion of Rule 24.2(b) and Note 6 on Rule 24.2 and the related amendments?

45. We would observe that in the case of cash offers the proposed amendments will not have significant benefits.

46. We also suggest that the Panel leaves provision in the rules to dispense with some of the financial disclosure requirements in certain circumstances. In particular when complying with proposed Rule 24.3(a)(vi) may be onerous for an unlisted foreign company and may deter a bidder, or the costs of compliance may reduce offeree shareholder consideration.

Q21 Do you have any comments on the proposed new Rule 24.3(a) and the related amendments?

47. We welcome the fact that references to “material” in Rules 24.2(a)(iv) and 25.2 are proposed to be changed to references to “significant” in order to bring the terminology into line with the PD Regulation. It would further improve consistency if reference to “subsequent to the date of its last published audited accounts” were replaced with “subsequent to the date of its last published audited accounts or interim statement”. This would ensure that the same statement would meet both prospectus and offer document requirements in situations where an offer document is issued after the publication of an entity’s interim statement and before the publication of the next annual accounts.

Q22 Do you have any comments on the decision not to require pro forma balance sheets to be included in offer documents?

48. We agree with this decision for the reasons set out in the PCP.

Q23 Do you have any comments on the proposed new Rule 24.3(c) regarding the disclosure of ratings and outlooks?

49. We have reservations on proposed new Rule 24.3(c) and would point out that there is no equivalent requirement in prospectuses for Class 1 transactions.

50. As a matter of principle, we question why the offeror and offeree should need to summarise and disclose opinions of ratings agencies (including changes) that they do not control and may not agree with. Such third party opinions should not be given factual status and any disclosure should be in their original form.

51. At the time of writing, there are over 70 rating agencies worldwide. We are concerned that the burden on companies will be significant and outweighs any benefits expected from disclosing ratings and outlooks. Less sophisticated shareholders may not be able to properly assess the weight of these.

52. We also question why rating agencies have been singled out as sources of independent information on the offeror and offeree while others, such as brokers and analysts, have not. Indeed given the state of progress on regulation of rating agencies and as well as discredited ratings they have given to companies, singling out this source of information may be premature.

Q24 Do you have any comments on the proposed new Rule 24.3(f)?

53. We agree with the proposed new Rule 24.3(f) but we do not agree that documents relating to the financing arrangements should be put on public display without redaction (para 6.34). This is commercially sensitive information that, as recognised in the case of "headroom" in a financing agreement, need not be disclosed (para 6.29).

Q25 Do you have any comments on the proposed new Rules 26.1 and 26.2 or the related amendments?

54. We have no comments.

PROVIDING GREATER RECOGNITION OF THE INTERESTS OF OFFEREE COMPANY EMPLOYEES

Q26 Do you have any comments on the proposed new Rule 24.2?

55. We have no comments.

Q27 Do you have any comments on the proposed new Note 3 on Rule 19.1?

56. We think that the first sentence in new Note 3 on Rule 19.1 should refer to "any particular course of action" as specified in para 7.9.

57. We agree with the principle behind the proposal. Given the prospect of disciplinary action, in situations where a bidder makes in good faith a statement that is either based on something the target board has told it and that turns out not to be true or is based on a macroeconomic outlook that subsequently changes, we would like to understand where the Panel believes the responsibility should lie.

58. We would also observe that the default 12-month period for adhering to a statement is restrictively long.

Q28 Do you have any comments on the proposed new structure for the obligations in relation to the publication, content and display of documents?

59. We have no comments.

Q29 Do you have any comments on the proposed new definition of "employee representative"?

60. We believe that para (b) to the new definition of "employee representative" should refer to persons formally or properly elected or who the offeror or offeree (as applicable) reasonably believes to be the properly elected person.

Q30 Do you have any comments on the proposed new Note 6 on Rule 20.1?

61. Since the new definition of employee representative is broader in scope, potentially including less sophisticated representatives, there is an increased risk of leaks even if the obligation on the offeror or offeree is to pass information "in confidence". It would be reasonable to require the relevant employee representative to sign a confidentiality agreement.

Q31 Do you have any comments on the proposed new Rules 2.12(a) and (d) and second sentence of Rule 32.1(b)?

62. A point of clarification would be useful in relation Rule 32.1(b); specifically on how the offeror or offeree would satisfy the obligation to "inform its employee representatives or employees of the right…". In view of para 7.22 would this obligation be satisfied by using the usual forms of communication with employees?

Q32 Do you have any comments on the proposed new Rule 25.9 and amendments to Rule 32.6?

63. We would observe that the proposed approach for dealing with an employee representative's opinion that is received late but within 14 days of the offer becoming or being declared wholly unconditional, renders the submission a somewhat procedural exercise, as by this stage the opinion will not be able to influence the outcome.

64. Note 1 to new Rule 25.9 is unclear on what constitutes 'reasonable' costs and the role of the Panel, if any, as arbiter of such costs.

Q33 Do you have any comments on the proposed new Rule 19.2(a)(iii)?

65. We have no comments.

MISCELLANEOUS AMENDMENTS

Q34 Do you agree that the suggested amendments to section 2(a) of the Introduction to the Code would be consistent with the amendments to the Code proposed in this PCP?

66. We agree.

Q35 Do you have any comments on the proposed new definition of "offer period"?

67. We have no comments.

Q36 Do you have any comments on the proposed new Rule 13.4?

68. We strongly believe that guidance is needed regarding new Rule 13.4(d) on the circumstances and factors that might prompt the offeror or its financial adviser to notify the Panel in order to prevent false 'red flags' from being raised. Guidance should cover the nature of information; the timing of notification and whether this should be after a period of time if circumstances may change; and the nature of any verification required to support the notification of changes.

69. Other practical considerations to address in guidance would include the action(s) the Panel will take upon receipt of such notifications and what the financial adviser's responsibilities are in the event the offeror disagrees with the adviser's assessment of the need for notification.

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