Impact of UK Takeover Code Reform - Seven Months On

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CLIFFORD CHANCE

Contents

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Impact of UK Takeover Code Reform – Overview

- Significant changes to the UK Takeover Code were introduced by the Panel on 19 September 2011 in an effort to address the perceived tactical imbalance which had arisen between prospective bidders and targets.
- Seven months on, we explore the impact of these changes and consider whether the landscape of UK public M&A deals has altered.

Before we look at the market data, here's a brief refresher on the key Code changes:

New Features	Summary of New Code Provisions
General prohibition on break fees and other deal protection measures	■ Total ban on break fees and inducement fees (except following a formal sale process or in favour of white knights after a firm intention announcement by a hostile bidder) ■ General ban on other deal protection measures (including non-solicitation of competing bidders and offer-related undertakings contained in implementation agreements)
Requirement to identify potential bidders	■ Requirement for target to identify all known potential bidders in any announcement it makes to start the offer period ■ Formalised 6 months "down tools" regime where bidder elects to walk away to avoid being identified (3 months with the target's support)
Automatic 28 day "put up or shut up" period (PUSU)	■ Automatic compulsory 28 day put up or shut up (PUSU) period starts to run from the public identification of each relevant bidder, within which the potential bidder must announce an offer or that it does not intend to make an offer
Enhanced disclosure in offer documentation	■ Transparency in relation to offer-related advisers' fees (including those incurred in bid financing) ■ Increased disclosure requirements regarding financing arrangements, bidder's plans for the target and other financial information in offer documentation

Key Take-aways

Our review of announcements relating to 56 target companies which entered an offer period between 19 September 2011 to 19 April 2012, revealed the following:

New Code Feature

Prohibition on break fees and other deal protection measures

Area of Impact	Key Take-aways
Break fees	No white knight fee has been agreed, but one formal sale break fee agreement[1] and two reverse break fee agreements have been disclosed.
Form of offer	No general shift to contractual offers, with schemes still being preferred on the larger deals.
Implementation agreements	A number of "co-operation agreements" have been entered into. "Co-operation agreements" are permitted under Rule 21.2(b)(iii) to the extent they relate to a commitment to provide information or assistance for the purposes of obtaining any official authorisation or regulatory clearance.
Irrevocable undertakings	There are indications that some deal protection measures (e.g. non-solicitation and matching rights provisions) are increasingly being seen in irrevocable undertakings.

Requirement to identify potential bidders and 28 day automatic PUSU

Area of Impact	Key Take-aways
Initial approach	Bidders appear to have exercised more caution and deliberation before initiating contact with the target as a result of the new PUSU rules.
Formal sale processes	A number of companies have put themselves into play by undertaking a strategic review of the options available and/or commencing a formal sale process.
PUSU extensions	PUSU extensions have been granted on a significant proportion of deals (in some cases with multiple extensions).

Enhanced disclosure in offer documents

Area of Impact	Key Take-aways
Bid financing	Although the Panel has agreed that headroom arrangements for a potential increased bid can be put in a side letter and do not need to be disclosed, market flex arrangements need to be disclosed under the new rules. However, market flex arrangements can be included in a separate market flex side letter and bidders have been allowed to defer disclosure from announcement until posting of the offer or scheme document.

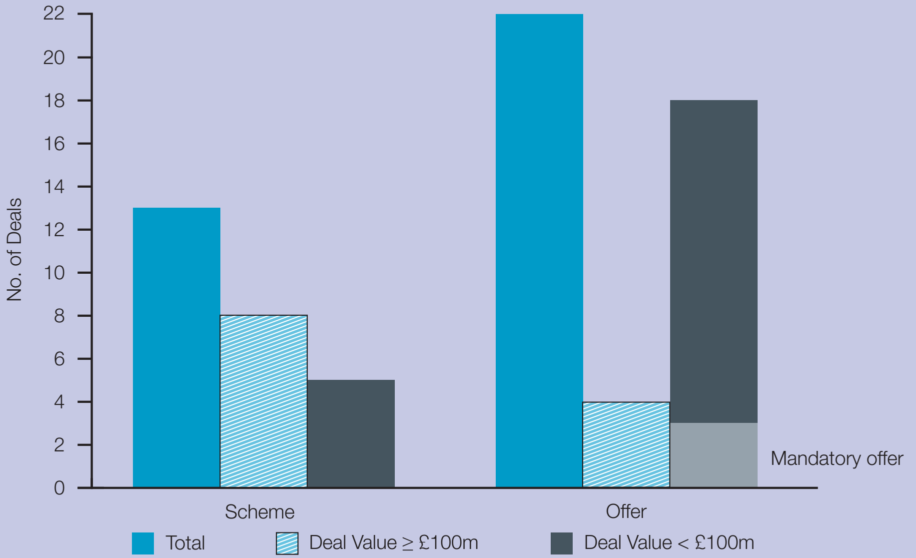
[1] The break fee agreement between Shell and Cove Energy was entered into on 24 April 2012. As Shell was a participant in a formal sale process, the Panel consented to the break fee agreement under Note 2 of Rule 21.2

Deal Landscape

56 target companies have entered an offer period since 19 September 2011

...with 35 Rule 2.7 "firm intention" announcements in the same period

Schemes appear to be favoured for £100m+ deals, whilst offers were favoured where the deal value was less than £100m



...of which 15 companies were put into play as a result of a strategic review and/or formal sale process initiated by the board

Outcome as of 19 April 2012

- Approximately 50% of which could be said to be in financial difficulties.
- One dispensation from the prohibition on break fees was granted[1].
- 3 named potential bidders and applied PUSU deadlines in the initial announcement, resulting in 1 Rule 2.7 "firm intention" announcement and 2 Rule 2.8 "no intention to bid" announcements[3].
- 10 sought dispensation from applying PUSU deadline.

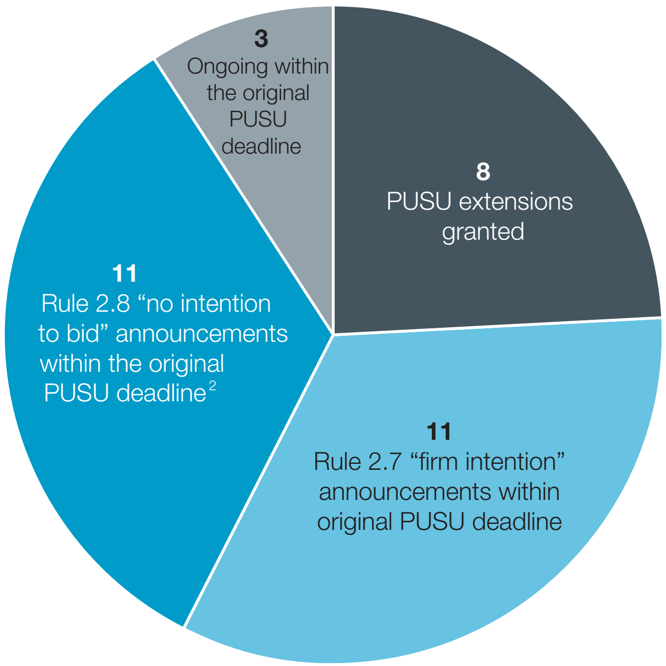
[1] The break fee agreement between Shell and Cove Energy was entered into on 24 April 2012. As Shell was a participant in a formal sale process, the Panel consented to the break fee agreement under Note 2 of Rule 21.2

[3] Includes one partial offer

PUSU Deadlines

33 approaches were subject to a PUSU deadline…

Outcome as of 19 April 2012



Of the 8 PUSU extensions:

- 3 had more than one extension
- 2 involved competing bidders
- 3 resulted in Rule 2.7 “firm intention” announcements
- 4 resulted in Rule 2.8 “no intention to bid” announcements
- 1 was still within the extended PUSU timetable as of 19 April 2012

[2] Includes one instance where the deadline was set aside as the target company entered into administration

PUSU Extensions

Looking at the 18 approaches in relation to in which the Panel has granted one or more PUSU extensions[3]:

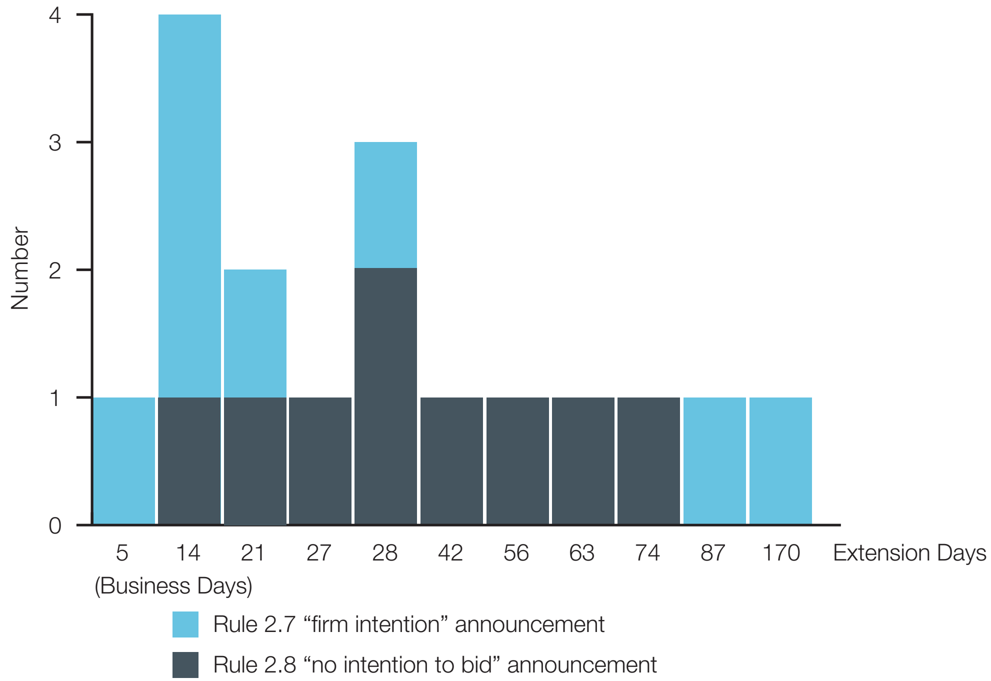
Outcome of PUSU extension as of 19 April 2012	Number
Rule 2.7 "firm intention" announcement	8
Rule 2.8 "no intention to bid" announcement[2]	9
Still ongoing within extended PUSU timetable	1

Longest extension?
54 days[4]

Shortest extension?
1 business day

Extension granted most often?
28 days

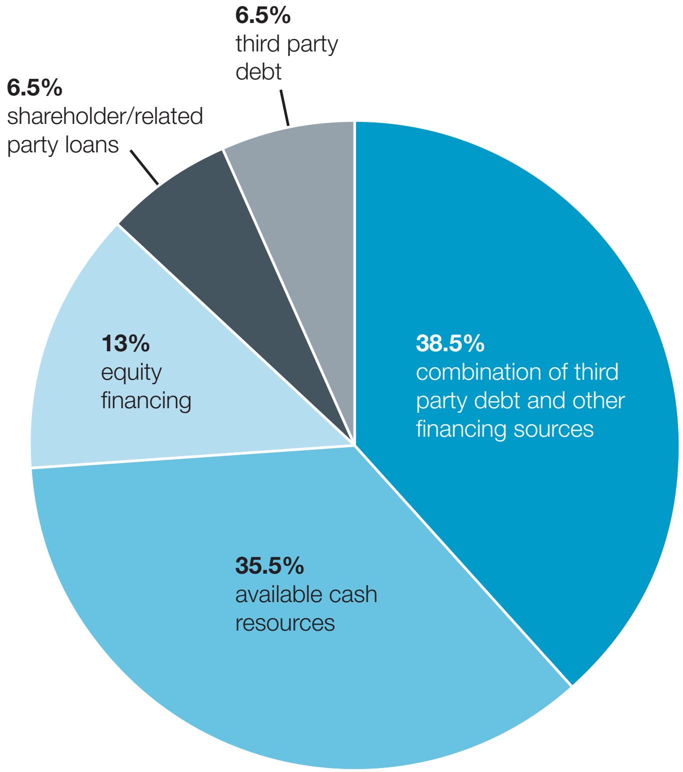
Length of extension v successful outcome?



[2] Includes one instance where the deadline was set aside as the target company entered into administration
[3] Includes companies which entered into an offer period prior to 19 September 2011
[4] STE (Clean Recycling & Energy) agreed a 54 day extension in relation to the possible offer by Spara Acquisition One Corp on 8 May 2012

Bid Financing

An analysis of the financing sources in relation to the 31 Rule 2.7 “firm intention” announcements of cash offers since 19 September 2011 reveals:



Whilst debt financing is still being used, particularly to fund the larger deals, many bidders are using alternative funding methods such as equity financing, shareholder loans and/or available cash resources.

Features of third party debt emerging from these deals include:

- dispensation from disclosing market flex terms until offer or scheme document posted;
- letters of credit used in several deals, a form of financing not previously seen in the UK public M&A sphere and which may permit less disclosure as the target shareholders are exposed to the issuing bank’s credit, rather than the bidder’s. This structure may potentially give corporate bidders an advantage; and
- a good proportion of deals were funded using short term or interim facilities, with a view to refinancing shortly after completing the offer.

[6] Excludes companies which entered into an offer period prior to 19 September 2011 and excludes all share offers, but includes cash and share offers and one partial offer

Summary

To recap, here's a quick snapshot of the data which we reviewed:

(1) 56 target companies entered an offer period between 19 September 2011 and 19 April 2012 (excluding companies which entered into an offer period prior to 19 September 2011):

- with 35 Rule 2.7 "firm intention" announcements in the same period:
  - of which 4 were all share offers and 31 were cash offers (including cash and share offers and one partial offer);
  - of which 13 were implemented using schemes of arrangement and 22 were contractual offers (including 3 mandatory offers); and
  - of which 12 had a deal value in excess of £100 million;
- of which 15 companies were put into play as a result of a strategic review and/or formal sale process initiated by the board:
  - resulting in 5 Rule 2.7 "firm intention" announcements (including one partial offer), 5 ongoing processes (as of 19 April 2012) and 5 terminated processes; and
- of which 33 approaches were subject to a PUSU deadline:
  - 3 of which were still ongoing within the original PUSU deadline as of 19 April 2012, and resulting in 8 PUSU extensions, 11 Rule 2.8 "no intention to bid" announcements, and 11 Rule 2.7 "firm intention announcements" within the original PUSU deadline.

    The 8 PUSU extensions ultimately resulted in 3 Rule 2.7 "firm intention" announcements and 4 Rule 2.8 "no intention to bid" announcements (including one instance where the deadline was set aside as the target entered into administration), whilst 1 was still ongoing within the extended PUSU timetable as of 19 April 2012.

(2) The Panel granted PUSU extensions in relation to 18 approaches in the period between 17 October 2011 and 19 April 2012 (including in relation to target companies which entered into an offer period prior to 19 September 2011):

- 1 of which was still ongoing within the extended PUSU timetable as of 19 April 2012, and resulting in 8 Rule 2.7 "firm intention" announcements and 9 Rule 2.8 "no intention to bid" announcements (including one instance where the deadline was set aside as the target company entered into administration).

Glossary

Implementation agreement	An agreement between a bidder and a target company pursuant to which the target company gives the bidder certain contractual commitments in relation to the implementation of a takeover offer. Prior to the recent Code changes, implementation agreements were standard practice on schemes of arrangement and were increasingly seen on contractual offers.
Letters of credit	A promise by the issuer to pay the beneficiary of the letter of credit in accordance with the conditions set out in that letter of credit (e.g. the presentation of certain specified documents). The letter of credit is issued by a bank at the request of the bidder (the applicant for the credit) in favour of the shareholders of the target company (the beneficiaries of the credit).
Market flex	Provisions in a syndicated loan agreement which allow the arranger to change the pricing and, sometimes, the terms and/or structure of the loan, if market changes make it necessary to do so in order to syndicate the loan successfully.
Reverse break fee arrangement	An arrangement entered into between a bidder or a potential bidder and a target company under which a cash sum would become payable to the target company by the bidder or potential bidder if certain specified events occurred which had the effect of preventing the transaction from proceeding or causing it to fail.

Save where expressly indicated, the information in this publication is as of, and is based on publicly available information as at, 19 April 2012.

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- Royal Dutch Shell on its recommended offer of £1.12 billion for Africa-focused Cove Energy plc
- International Power plc (IPR) in connection with the £6.4 billion recommended cash offer by Electrabel S.A., a wholly owned subsidiary of GDF SUEZ S.A., to acquire the ordinary share capital of IPR not already owned by GDF SUEZ
- SS&C Technologies Holdings, Inc. on its recommended £575 million (US$900 million) cash offer for GlobeOp Financial Services S.A.
- Dominion Petroleum in relation to its £139 million recommended takeover by Ophir Energy plc
- LCH.Clearnet Group Limited on the recommended cash offer by London Stock Exchange Group plc to acquire a majority stake in LCH.Clearnet (valuing it at €813 million)

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