

C L I F F O R D

C H A N C E



**LIABILITY MANAGEMENT
KEY CONSIDERATIONS FOR DEBT ISSUERS
IN ASIA PACIFIC – 2ND EDITION**

INTRODUCTION

The existence of quantitative easing and a low-interest rate environment have been significant contributors to record volumes of debt issuance across a variety of currencies by a wide range of corporate and sovereign issuers in the Asia Pacific (ex-Japan) region in recent years.

Since the publication of the 1st Edition of *Liability Management – Key Considerations for Debt Issuers in Asia Pacific*, there has been increasing volatility in various currency markets driven by recent U.S. federal reserve rate increases (with further rate increases having been signalled to occur through the end of 2018 and in the course of 2019) and an appreciating US dollar, as well as resulting from shifts in U.S. trade policy and continuing volatility in Sterling and euro currency markets post-Brexit in 2016.

Against this backdrop, there has been a progressive increase in bond defaults since 2016, with approximately S\$1 billion (approximately US\$730 million) in defaulted debt by oil services sector issuers alone in the Singapore dollar market and almost US\$5 billion in bond defaults by Chinese corporate issuers in 2018 thus far (according to *Bloomberg*, who have also identified US\$18 billion in bond maturities by Chinese property developers falling due in the first quarter of 2019).

As such, companies which have a significant degree of capital markets debt on their balance sheets and facing financial distress as a result of uncertain economic circumstances may also be forced to reassess their capital structure and engage with creditors (including bondholders) early in order to stave off or cure impending or existing defaults or insolvency scenarios or, more proactively, seek to optimise their balance sheet position.

Other than in the context of distress, liability management techniques can also be used by healthy companies to optimise their capital structures (through deferring near-term maturities or achieving deleveraging efficiencies) or otherwise actively mitigate risks where, for example, covenants in existing bond conditions are or will come under stress (for example, in the context of a leveraged acquisition), and a threat of future breaches exists which could lead to events of default under the terms of the bonds and resulting in cross-defaults across an issuer's debt capital structure.

In addition, the regulatory environment governing access to the international debt capital markets has continued to evolve (for example, with the adoption of the EU Market Abuse Regulation, MiFID II and recent changes to the SGX Listing Manual), presenting new challenges for issuers, investment banks and financial institutions active in international and regional fixed income markets in the region, but also offering potentially rewarding opportunities for issuers in the region to take an active approach to the management of outstanding liabilities, and the rebalancing of corporate balance sheets.

This document describes the main techniques which issuers in the region, who are considering liability management either in the context of an active debt capital restructuring exercise or financial distress situation, might employ. It also highlights some of the legal issues that they and their financial advisors will need to take into account. This 2nd Edition seeks to highlight some recent changes in the regulatory landscape and highlight new developments and techniques in liability management transactions.

This document assumes that a liability management exercise will be undertaken in respect of an initial bond issue placed with professional or institutional investors, and does not seek to address issues specific to retail bond markets in the Asia Pacific region.

Matt Fairclough
Partner, on behalf of the
Asia Pacific Debt Capital Markets Group

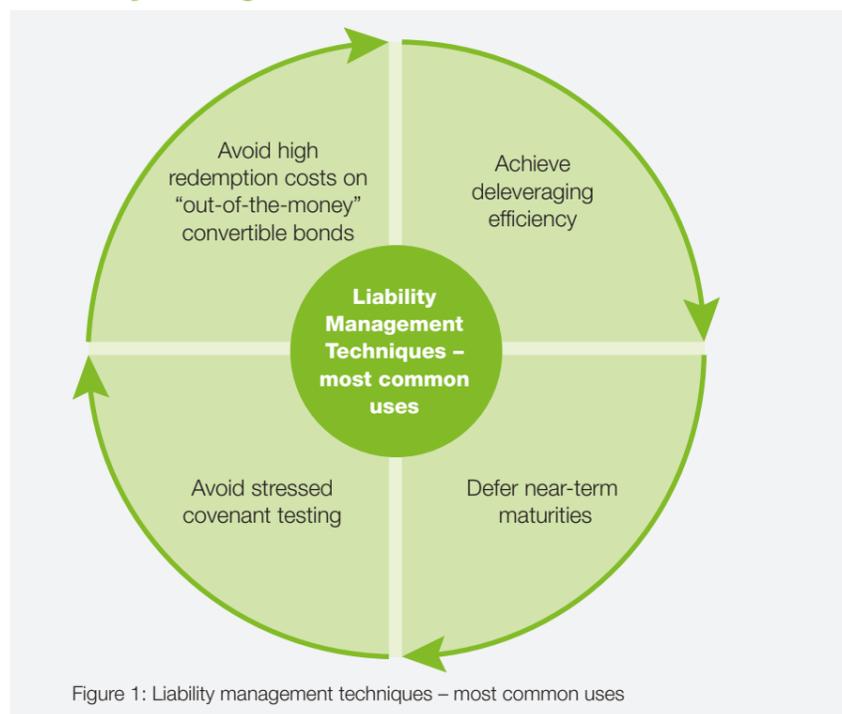
Johannes Juette
Partner, Co-head U.S. Securities Practice,
Asia Pacific

Gareth Deiner
Partner
Debt Capital Markets

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1. What is liability management and why undertake a liability management exercise?



One of the fundamental differences between capital markets (or “bonds”) and traditional bank debt (or “loans”) lies in the tradeability of bonds as securities: unlike bank debt, borrowers (i.e. issuers of debt securities) in the international capital markets do not typically know who their creditors are from one day to the next, given that a global security represents the aggregate principal amount of the issue is registered in the name of (in the case of registered bonds), or held by a nominee for (in the case of bearer bonds), the relevant clearing system.

Accordingly, the term “liability management” is used to describe a variety of procedures and techniques used by debt capital markets issuers for the purposes of buying back, exchanging or altering the terms of outstanding bonds in order to restructure – or “manage” – their balance sheet liabilities, in light of the difficulties inherent in seeking to restructure capital markets debt given the anonymity of bondholders.

These liability management techniques include tender offers (a “public” offer made by an issuer to repurchase all or a portion of its outstanding bonds from investors for cash), exchange offers (an offer made by an issuer to repurchase its outstanding bonds in exchange for new bonds with different terms), consent solicitations (a proposal made by an issuer to its bondholders for amendments to the terms of its existing bonds) or open market repurchases (which are typically privately negotiated and opportunistic repurchases of bonds by an issuer in the open market).

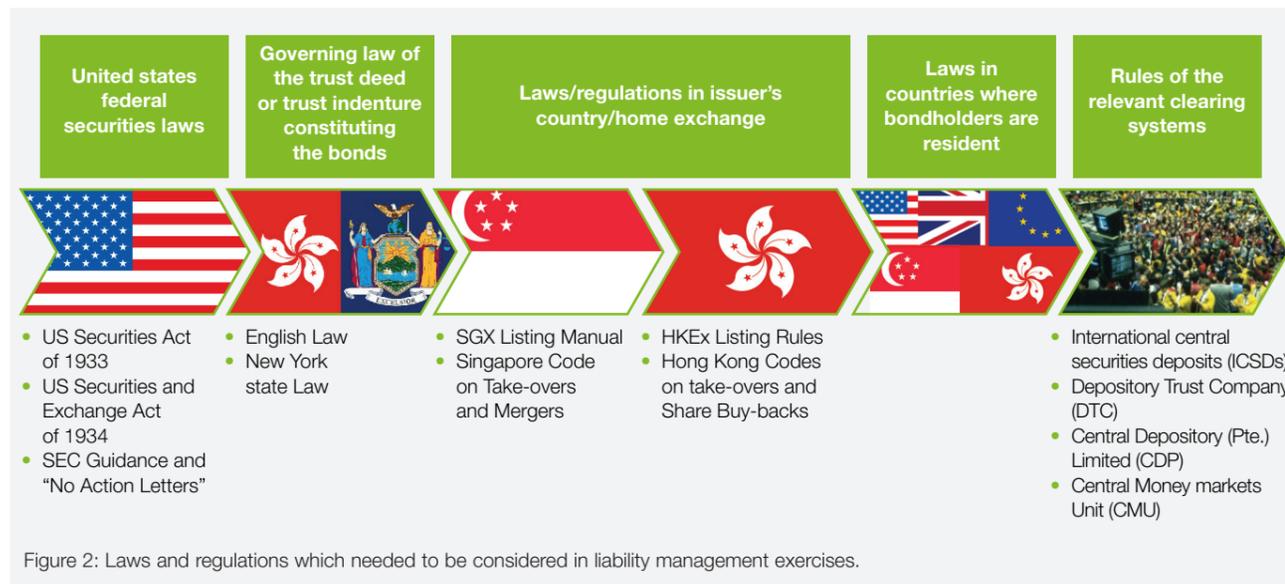
Each of these techniques can also be, and frequently are, combined to maximise the prospects of success of the principal liability management exercise. For example, an exchange or tender offer is frequently combined with a consent solicitation (in a process known as an “exit consent”) which seeks to incentivise bondholders’ participation in the overall transaction by requiring their consent to the proposed amendments as part of the tender of bonds pursuant to the tender offer or exchange offer. See “*Liability Management Techniques – Consent Solicitations*”, below.

Undertaking a liability management exercise is an important part of, but not limited to, distressed debt situations. One or more of the liability management techniques outlined above (and described in more detail in this document) can be used by bond issuers to:

- *Achieve deleveraging efficiency* – Where outstanding bonds are trading at significant discounts as a result of decreases in secondary market prices, an issuer may be able to optimise its leverage by repurchasing bonds (through a tender offer or open market repurchases) with cash-on-hand and cancelling them at relatively cheap prices. In addition, issuers may consider swapping bonds denominated in one currency for bonds denominated in another currency, where hedging costs and the cost of capital may prove cheaper, and investors are actively seeking exposure to that other currency;
- *Defer near-term maturities* – Where outstanding bonds are maturing in the near-term, issuers can seek to extend their maturity by offering to exchange them for a new series of longer-dated bonds;
- *Avoid stressed covenant testing* – Where existing covenants are, or may come, under pressure as a result of macroeconomic, strategic commercial or business-specific circumstances, issuers can seek a waiver or amendment of such covenants through a consent solicitation. In addition, issuers who are anticipating making acquisitions in the near future (which could effectively be prohibited under the terms of existing bond covenants) may look to replace longer term, inflexible capital markets debt with medium term, more flexible bank debt;
- *Avoid high redemption costs on “out-of-the-money” convertible bonds* – Where an issuer has convertible bonds outstanding and is facing unexpected redemption costs as a result of bondholders being unlikely to convert their bonds into shares (as the issuer may have expected), issuers may consider an exchange offer of existing convertible bonds for bonds with new terms which will serve to both alleviate their immediate cash flow difficulties and retain the confidence of their investors.

In addition, investors tend to perceive favourably an active approach by issuers to balance sheet liability management, giving them the opportunity to engage directly with issuers to consider restructuring opportunities, gain access to enhanced liquidity in the bonds being traded, avoid a technical default scenario or promote their position in the capital structure of an issuer. As such, an active approach to liability management may have the added benefit of enhancing an issuer’s profile in international debt capital markets generally.

2. Which laws need to be considered?



Any liability management exercise will typically involve the laws of a number of different jurisdictions, depending on the circumstances of each transaction, as follows:

United States federal securities laws

At the outset, it is important for an issuer to try to establish the proportion of its bonds held by U.S. investors because, if a tender or exchange offer is to be made to U.S. holders of the bonds, the issuer is likely to need to comply with U.S. tender offer rules under section 14 of the U.S. Securities Exchange Act of 1934 (the **"US Exchange Act"**) and Regulation 14E promulgated thereunder (known collectively as the **"Williams Act"**).

In essence, section 14(e) of the US Exchange Act makes it unlawful to engage in any fraudulent, deceptive or manipulative acts or practices in connection with any tender offer (including an exchange offer) and empowers the U.S. Securities and Exchange Commission (the **"SEC"**) to define and prescribe means that are designed to prevent such acts or practices. The SEC has accordingly done so through the legislative instrumentality of Regulation 14E. Below is a summary of some of the principal requirements of such Regulation that need to be satisfied for a tender offer made to US holders:

(1) The 20 business day rule

Rule 14e-1 requires that a tender or exchange offer must be held open for at least 20 business days from the date that the offer is first published or sent or given to bondholders.

(2) Extension of the offer period and changes to the terms of the offer

Rule 14e-1(b) requires that the tender or exchange offer must remain open for a further period of at least 10 business days after any amendment is made to the offer price, or the percentage of the class of bonds being sought in the offer, or the

dealer's soliciting fee. Further, Rule 14e-1(d) requires that if any other change is made to the terms of the tender or exchange offer, the offer must remain open for a further period of at least five business days.

(3) The prompt payment rule

Rule 14e-1(c) requires that the offeror must pay the consideration offered, or return (or unblock) the tendered bonds, "promptly" following the termination or withdrawal of the tender or exchange offer. What constitutes such "prompt" action is not defined in the rules, however, the SEC staff has issued guidance to the effect that the payment of funds and the delivery or unblocking of bonds no later than the third business day after such termination or withdrawal would fall within the requirements of Rule 14e-1(c), having regard to the practices of the financial community and current settlement practices.¹

(4) Notice of extension of offer period

In the event that the offer period is extended, Rule 14e-1(d) requires the offeror to disclose such extension through a press release or other public announcement, which also needs to disclose the approximate level of acceptances of the offer to date. For securities listed on the Singapore Exchange Securities Trading Limited (the **"SGX"**) or The Stock Exchange of Hong Kong Limited (the **"HKEx"**), this would include uploading the appropriate announcement on the relevant exchange's website, as well as issuing a press release through a news service such as Bloomberg.

(5) The "best price" rule

Rule 13e-4(f)(8)(ii) requires that the consideration paid to any security holder for securities tendered in the tender offer be the highest consideration paid to any other security holder for securities tendered in the tender offer. As a technical matter, it is commonly accepted that the best price rule does not apply to "straight" debt securities (and only to tender offers for equity securities), however, it is followed in practice in U.S. tender offers, with Dutch Auctions (see *"Liability Management Techniques – Tender Offers"*, below) not being used in order to avoid breaching this rule.

A more detailed consideration of relevant U.S. tender offer rules and securities laws is outside the scope of this document but, because of the requirements they impose, if the proportion of the relevant securities held by U.S. persons is not significant their participation is typically excluded from any tender or exchange offer.

In determining whether or not to exclude the participation of U.S. persons from a tender or exchange offer, where the original placement included a resale under Rule 144A of the U.S. Securities Act of 1933 (the **"U.S. Securities Act"**), the question of whether or not to structure the offer in compliance with the U.S. tender offer rules may be obvious, but issuers should understand that, even where the bonds were originally distributed under Regulation S of the U.S. Securities Act, a significant portion of those bonds may have flowed into the U.S. or to U.S. persons in the secondary market following the initial issuance of the bonds.

While it is possible in certain circumstances to avoid the onerous requirements and application of the U.S. tender offer rules by excluding U.S. investors from the proposed tender or exchange offer, if the proportion of the relevant securities held by U.S. persons is significant (and exclusion of U.S. investors from the offer would likely prejudice the commercial success of the transaction), it will be necessary to comply with the U.S. tender offer rules highlighted above and other U.S. securities laws such

as the anti-fraud provisions of Section 10(b) and Rule 10b-5 of the U.S. Exchange Act (particularly where an exchange offer includes the placement of new securities).

However, the SEC's Division of Corporation Finance issued a "No Action Letter"² which has had the effect of creating a category of accelerated tender offers for non-convertible debt securities that can be held open for as little as five business days in certain circumstances. The specific requirements of the five-day tender offer rule are discussed in further in detail under "*The Accelerated US Tender Offer*", below.

Governing law of the trust deed or trust indenture constituting the bonds

Issuers will need to have regard to the governing law of the transaction documents under which their bonds were initially issued. For major cross-border international bond issues, particularly in the Eurodollar bond market, the two most prevalent governing laws are English law (typically governing transactions for bond issues sold to investors outside of the U.S. in reliance on Regulation S) and New York state law (typically governing transactions for bond issues sold to investors where part of the offering includes a placement under Rule 144A). As will become apparent from this document, specific features and nuances of the relevant governing law of the documents constituting the bonds (a trust deed under English law and a trust indenture under New York state law) will need to be taken into account in structuring a liability management exercise, as the same legal regime will likely govern the terms of the liability management exercise. In particular, and as a first step in the structuring of any liability management exercise, a careful analysis of the terms and conditions of the bonds and the provisions of the trust deed, or indenture, constituting the bonds needs to be undertaken to ensure that the structure of the liability management exercise is permitted by the terms of the bonds. This applies both to consent solicitation exercises, where the trust deed will set out certain thresholds for the passing of ordinary or extraordinary resolutions depending on the term for which an amendment or waiver is sought, and to tender offers, where any repurchase of bonds is required to be permitted by the terms and conditions of the bonds. See "*Specific legal considerations applicable to liability management exercises – Are repurchases specifically permitted under the existing bond terms and conditions?*" below.

Applicable laws in the issuer's country and the regulations of the exchange on which the bonds are listed

Apart from the federal securities laws of the United States and the governing law of the bond documents, an issuer considering some form of liability management exercise will need to be aware of applicable laws in its own country and the regulations of the stock exchange on which its bonds are admitted to trading.

For example, issuers with bonds listed on the SGX are subject to continuing obligations under the SGX Listing Manual, which requires an issuer to disclose immediately to the SGX any information which may have a material effect on the price or value of its debt securities or on an investor's decision whether to trade in such debt securities.³ In addition, and following amendments made to the SGX Listing Manual on 6 May 2016, an issuer is now required to immediately announce the redemption or cancellation of its debt securities, when every 5 per cent. of the total principal amount of those securities (calculated based on the principal amount at the time of the initial listing) is redeemed and cancelled.⁴ See "*Specific legal considerations applicable to*



liability management exercises – "Creeping" tender offers and the risk of integration in open market repurchases", below.

Similar continuing obligations are imposed on issuers with bonds listed on the HKEx. Rules 37.44 to 37.53 of the HKEx Listing Rules set out these continuing obligations and, in particular, require an issuer to immediately (after consultation with the HKEx) announce any information which is necessary to avoid a false market in its listed debt securities where, in the view of the HKEx, there is or there is likely to be a false market in its listed debt.⁵ Similarly to the SGX, the HKEx Listing Rules also require an issuer to announce as soon as possible aggregate redemptions or cancellations of bonds which exceed 10% (and every subsequent 5% interval) of an issue,⁶ and to notify the HKEx in advance of any proposal to replace a trustee for bondholders or to amend the trust deed or the bonds.⁷

In the case of convertible bonds which are admitted to trading on a different stock exchange from that on which the underlying shares are listed, an issuer will also need to take account of the laws of the country of that stock exchange, plus any applicable stock exchange or listing authority rules applicable to its equity. For example, in relation to convertible bonds where the underlying shares (into which the bonds are convertible) are listed on the HKEx, the issuer and its advisers will need to conduct an analysis under the Codes on Take-overs and Share Buy-Backs issued by the Hong Kong Securities and Futures Commission and, where such shares are listed in Singapore, under the Singapore Code on Take-overs and Mergers.

In addition, United Kingdom securities laws, such as the Financial Services and Markets Act 2000, will be relevant if offers are likely to be made in, to or from the United Kingdom.

Further, the adoption of Regulation 596/2014 of the European Parliament and of the Council of the European Union (the "**Market Abuse Regulation**", or "**MAR**") on 3 July 2016 has had the effect of extending the scope of the EU's market abuse regime to EU multilateral trading facilities or "**MTFs**". Accordingly, where an issuer has securities admitted to trading on a regulated market or MTF in Europe, any liability management exercise (particularly a tender offer, open market repurchase or exchange offer) is likely to be impacted by the key obligations imposed by MAR. See "*Market abuse and insider trading considerations – Market abuse and the implications of MAR*", below.

Laws in countries where bondholders are resident

In the context of an exchange offer or tender offer, an issuer will need to consider applicable laws in countries where bondholders are resident. An issuer and its advisers may have a fair idea of the location of significant holdings and may decide to initiate a holders search to try to provide more clarity. Given that most bonds are held in clearing systems, it is unlikely ever to be possible to ascertain precisely the exact identity of the investor base. It is usual, however, to exclude participation by holders in certain countries where local requirements are relatively onerous (notably the U.S. and Italy⁸) in cases where investors are not sufficiently numerous in those countries as to make the potential benefits of compliance outweigh the costs for some processes.

In the context of consent solicitations, it should be noted that bondholders cannot be excluded from participating in any consent process seeking to amend the terms of bonds which they own. However, as a consent solicitation does not involve the offer or

sale of bonds, it does not require registration under the U.S. Securities Act and is otherwise not subject to the anti-fraud provisions of U.S. federal securities laws or similar antifraud or market abuse laws in Europe, thereby being of less concern from a securities regulation perspective, and minimising the commercial or practical need to exclude holders in certain jurisdictions. However, care does need to be taken to ensure that any proposed amendments to the terms of the bonds do not “substantially affect” the rights of bondholders, namely, that the amendments may be deemed to constitute the offering of new securities. See “*Specific legal considerations applicable to liability management exercises – Consent solicitations and the ‘new security’ doctrine*”, below.

Rules and procedures of the relevant clearing systems

While not strictly speaking a matter of law, consideration also needs to be given to the relevant rules and procedures of the clearing systems through which the bonds to which the liability management exercise relates are cleared.

Typically, bond issues denominated in U.S. dollars are cleared through the International Central Securities Depositories (or “**ICSDs**”, being Euroclear and Clearstream) (in the case of a Regulation S only offering), and the Depository Trust Company, or “**DTC**” (in the case of a Rule 144A placement), while bond issues denominated in Singapore dollars are usually (but not necessarily) cleared through the SGX’s Central Depository (Pte.) Limited, or “**CDP**”, and bond issues denominated in Hong Kong dollars are usually (but not necessarily) cleared through the Hong Kong Monetary Authority’s Central Moneymarkets Unit system, or “**CMU**”.

While the clearing system through which the bonds trade and settle is unlikely to have any substantive impact on the structuring considerations for a liability management exercise, it is important to note that different clearing systems will have different processes in supporting the paying and tabulation/exchange agent through the exercise. Accordingly, the principal difference between the ICSDs and local clearing systems like the CDP and the CMU is that the ICSDs have automated processes and electronic platforms which support critical functions in a liability management exercise, whilst the local systems do not, meaning that the agents will need to manually support these functions in the course of the exercise. A summary of some of the principal differences between the ICSDs and DTC, on the one hand, and local central securities depositories (such as CDP and CMU), on the other is as follows:

(1) Communication

The ICSDs and DTC are set up to facilitate automated communication with participants and holders. For example, the ICSDs create and distribute a DACE⁹ notice and facilitate the electronic transmission of the invitation document.¹⁰ In the case of DTC, this includes the creation and distribution of a summary notice, and the provision of access to an “e-platform” for all parties. By contrast, for CDP and the CMU, no automated notices are prepared and distributed, and the principal invitation document needs to be physically posted or electronically emailed to the system participants. Similarly, only the first level of holders is capable of being ascertained (for example, holders with direct accounts in CDP or CMU, or nominees for other holders) which, in turn, impacts the timing and production of position reports for the liability management exercise. Furthermore, the ICSDs and DTC are able to support reconciliation of final positions with the agent via SWIFT, as well as provide automated communications to

all holders, whereas these functions would need to be manually carried out by the issuer through its agents in CDP and CMU;

(2) Voting and Blocking

While the ICSDs, DTC and CDP are capable of automatically blocking positions upon receiving instructions,¹¹ CMU does not have a similar mechanical concept, meaning that, in circumstances where positions in bonds need to be blocked (principally, where positions are voted), a manually supported escrow mechanic will need to be devised, and where the constitutive instrument for the bonds (e.g. the trust deed) precludes the voting of bonds held beneficially for the issuer, a declaration of trust will also be required to prevent the exclusion of the bonds so escrowed from voting. This process, including the escrow agency and trust mechanics, all require manual support from the agent in addition to being formally documented.

(3) Funds Settlement

The ICSDs and DTC are able to fund holders directly (for example, in the case of settling the purchase price for a tender offer or the payment of consent fees), whereas similar payments for bonds cleared through CDP and CMU need to be manually supported by the agent.

(4) Formal Notices

For bonds cleared through the ICSDs, it is typical for the underlying bond documentation (normally, the global note or global note certificate) to provide that, while such bonds are held in global form, any notice to holders is validly given if delivered to the ICSDs, as issuers can communicate directly with bondholders through the electronic platform provided by the ICSDs. This eliminates the need for the physical publication of notices in newspapers having general circulation in the jurisdiction of the issuer and/or the listing venue of the bonds. As local systems such as CDP do not have a similar electronic communication platform, it remains necessary for issuers to publish notices of meetings (and for other notice obligations to be performed under the terms and conditions of the bonds) in the newspapers provided for in the notices condition in the terms and conditions. Differences such as these in the settlement systems will have a significant bearing on the timeline for any proposed liability management exercise and are important to consider for the purposes of both composing the timetable, and the selection of the tabulation or exchange agent (to ensure they have sufficient experience of the manual support required), for the exercise.



3. Liability Management Techniques

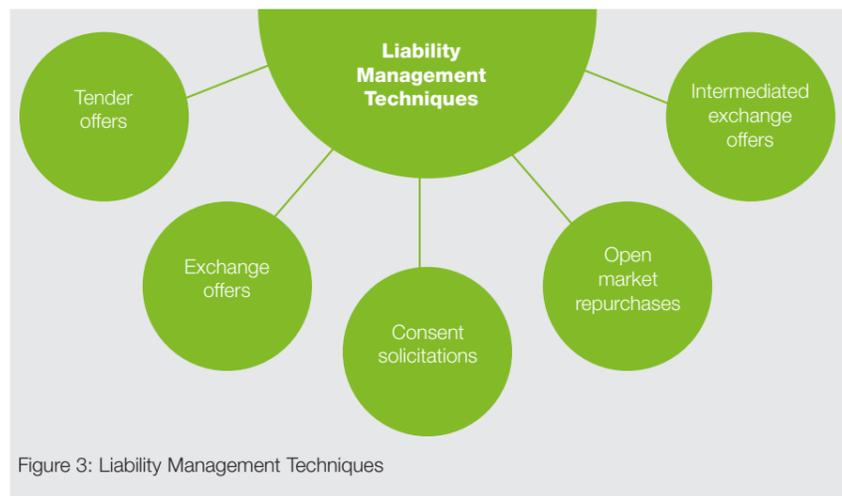


Figure 3: Liability Management Techniques

Tender offers

An issuer with bonds outstanding in the international capital markets may decide to make an offer to purchase its bonds by launching a public offer for the debt. Such an invitation allows an issuer to retire a significant portion of a particular bond issue. With the exception of the U.S. tender offer rules highlighted above, which prescribed fixed time periods for the offer to remain open, there are no rules prescribing a minimum or maximum duration of the offer period: as a practical matter, it must be sufficiently long to allow for distribution of materials through the clearing systems and for investors to respond. In many cases, issuers will opt for an offer period of 7-10 business days. Issuers may choose to price the tender on a fixed basis at the outset (which has the benefit of simplicity) or opt for a spread over a reference rate (priced towards close of the offer) which goes some way to transferring the risk of price movements to investors. Alternatively, issuers may consider so-called “Dutch Auctions”, where investors are invited to bid at a price (usually within a specified range), and the issuer accepts such bids at individual prices for the level of buy-back it wishes to achieve. Owing to the best price rule, this technique is generally viewed as being impermissible for tender offers that are subject to the U.S. tender offer rules. Alternatively, issuers may use so-called “modified Dutch Auctions” where bids at the clearing price are accepted pro rata if acceptance in full would result in the issuer purchasing more bonds in aggregate than the overall limit (if any) set by the issuer in the invitation to tender.

An issuer will normally appoint an investment bank with experience in liability management transactions to act as “dealer manager”. Usually, a tender offer memorandum or invitation will be produced, describing the terms of the offer, the applicable restrictions on participation and the means by which a beneficial owner of bonds may accept the offer. In respect of bonds which are admitted to trading on the SGX or HKEx, there is no requirement for any review or approval of the tender offer memorandum or invitation by any competent authority. The tender offer may be

launched by posting a notice through the clearing systems (if the clearing system in question has the necessary communications platform), and, in the case of bonds admitted to trading on the SGX, publishing a simultaneous announcement through the SGXNet portal or, in the case of HKEx listed bonds, on HKExnews. Particular care should be taken to ensure that notices and distributions of offer material comply with applicable laws and stock exchange or listing authority rules, such as the continuing obligations for SGX-listed bonds described above.

Exchange offers

An exchange offer typically involves an offer by the issuer to the holders of outstanding bonds to exchange those bonds for an amount of newly-issued bonds. The offer may be made in respect of all or part (for example, up to a maximum amount) of the outstanding bonds. This technique allows an issuer to extend the maturity of outstanding bonds or effectively amend their terms, whilst at the same time retaining substantially the same investor base (which is familiar with the issuer and its credit profile). The economics of the offer (for example, the coupon or covenants applicable to the new bonds) will vary depending on the individual position of the issuer, its objectives in undertaking the exchange offer and the prevailing trading climate.

Unlike a public cash tender offer described above, an exchange offer involves the issue of new bonds and, usually, their listing and admission to trading on a stock exchange. Bearing this in mind, an issuer will need to take particular care to comply with applicable legal and regulatory requirements in the jurisdictions where existing holders are resident as offers of new securities are generally much more heavily regulated than offers to buy existing bonds for cash. Again, it is usual to exclude participation by holders in certain countries where local requirements are relatively onerous (notably the U.S. and Italy) in cases where investors are not sufficiently numerous in those countries as to make the potential benefits of compliance outweigh the costs.

Documentation for an exchange offer typically includes a dealer manager agreement (appointing an investment bank as dealer manager) and an exchange offer memorandum which describes the terms of the offer and, importantly, contains disclosure on the terms of the new bonds and the issuer. Where the new bonds are to be admitted to trading on a stock exchange such as the SGX, an offering circular (describing the terms of the new bonds, together with the related business, risk and financial disclosures applicable to the issuer) will be appended to the exchange offer memorandum, and will comprise the “offering document” which will be subject to the usual approval by the stock exchange for listing purposes. Given the additional complexity and, in particular, the time required to produce the offering circular, issuers will usually need to allow a significantly longer preparation time prior to launch than would be the case for a public cash tender offer.

Consent solicitations, mandatory exchanges and exit consents

Issuers may consider launching a consent solicitation whereby a proposal is put to bondholders to consider an amendment to the terms of outstanding bonds. Under a bond issue constituted by an English, Hong Kong or Singapore law trust deed, this may also involve convening a meeting of bondholders to consider and vote on the proposals for amendments. A consent solicitation may be done to avoid a potential breach of a particular covenant, to cure or waive breaches or events of default that

have already occurred, or to introduce new terms such as a “call” option allowing the issuer to redeem the bonds prior to their stated maturity at a specified price.

The advantage of obtaining the approval of bondholders by an extraordinary resolution is that it binds the entire class of bondholders: in other words, it is possible, provided necessary quorum and voting thresholds are met, to retire an entire series of bonds. In addition, a consent solicitation can also be used to request holders to sanction a mandatory substitution or exchange of an entire series of bonds for another (where the rules and procedures of the relevant clearing system permit and the meetings provisions of the bonds expressly provide holders with the power to do so). However, the “cram down” effect of the mandatory exchange technique is seldom used in a commercial context, given the potential for alienating minority holders (who may otherwise not have participated in an exchange offer, or who would have preferred to be cashed out of their positions in the bonds, for example by way of an exchange offer with an exit consent – see below) and thereby potentially making future market access difficult, and is likely only appropriate in specific distress scenarios where other alternatives are not feasible in a restructuring context.

Tender offers and exchange offers may also be combined with a bondholder meeting where the holders are invited to consider an extraordinary resolution to give the issuer a right to call the bonds early (often called an “exit consent”). Bondholders who accept the offer also automatically deliver an irrevocable instruction to vote in favour of the extraordinary resolution. Provided the necessary quorum and voting requirements are satisfied, the issuer is then able to redeem the entire series of bonds either for cash or for a combination of cash and new securities. However, care needs to be exercised to ensure that modifications made to the terms of the existing bonds as part of the exit consent do not impose unfair or punitive outcomes on dissenting or non-participating bondholders (see “*Specific legal considerations applicable to liability management exercises – equal treatment of bondholders and oppression of the minority in exit*”).



consents”, below, for a detailed discussion of these considerations). Where the extraordinary resolution is not passed at a meeting of bondholders, the issuer may decide to accept for redemption that portion of bonds held by holders who have accepted the offer and leave outstanding the remainder of the series.

The exit consent and the mandatory exchange is a useful technique for an issuer to consider where it is imperative that an entire class is retired, as would be the case, for example, where the motive for the offer and solicitation is to remove a “problem” covenant. Where an exchange offer or cash tender offer is combined with a consent solicitation, the notice requirements for a meeting (typically 21 days, as set out in the meeting provisions in the trust deed constituting the bonds) will need to be observed and this will have an impact on the duration of the applicable offer.

Open market repurchases

An issuer may consider repurchasing a modest portion of its outstanding bonds on a case-by-case basis, by taking bids from participants in the secondary market. Alternatively, an issuer may mandate a bank to execute such repurchases on its behalf. This technique allows an issuer to retire a portion of a bond issue in a relatively low-key manner. However, careful consideration should be given to applicable regulatory issues,¹² particularly in relation to market abuse and insider trading. See “*Market abuse and insider trading considerations*”, below.

Intermediated exchange offers and switches

An intermediated exchange offer (also known as an intermediated tender offer) is a technique which combines a tender offer with an issue of new bonds. Intermediated exchange offers have been used successfully in European bond markets in order to achieve exchange accounting treatment, i.e. where existing bonds are trading above their par value, any premium paid for them in a tender can be amortised over the life of the new bonds issued under exchange accounting rules in the issuer’s home jurisdiction and under the accounting principles applicable to the preparation of its financial statements. The dealer manager, as offeror, is required to act as the intermediary in order for the exchange to work and achieve exchange accounting treatment. While exchange accounting treatment may not always necessarily be available to issuers in Asian jurisdictions and markets, intermediated exchange offers are increasingly being used in order to allow issuers and their bankers to execute a transaction on an accelerated basis (with the tender and the new issue process being executed on the same day), and minimising exposure to market volatility that may otherwise adversely impact a successful tender or exchange if left open for a longer period of time.

An intermediated exchange offer is documented and executed as a tender offer with a new bond issue taking place contemporaneously. The dealer manager will take the role of offeror in the tender offer, and pay the purchase price to holders whose bonds are accepted for sale. The tender offer is therefore a third party offer (i.e. not made by the issuer or a member of its group). The purchase price that the offeror pays for the new bonds is financed from the proceeds of the new bond issue.

The documentation is largely the same as that for a tender offer coupled with a new issue, except that the dealer manager will enter into an exchange settlement

agreement with the issuer, which will document the agreement between the issuer and the dealer manager for the exchange of the old bonds for new bonds, taking into consideration the differential between the purchase price of the old bonds and the issue price of the new bonds (and fees).

From a risk perspective, it is important to note that the dealer manager will assume credit risk on the old bonds for a period equal to the difference in the time between the settlement of the tender offer and the issuance of the new bonds. Accordingly, it is important that the timing of the settlement of the tender offer and the new issue are aligned as closely as possible.

By contrast, a switch transaction is structured very similarly to an intermediated exchange offer, except that the tender offer is made directly by the issuer, and not a third party intermediary. While used by sovereign issuers in Asia in the past, care needs to be exercised should a corporate issuer consider such a direct switch transaction because, depending on the accounting standard under which it reports, it may not benefit from the same exchange accounting treatment that an intermediated exchange would otherwise provide.

Care will also need to be exercised to ensure that appropriate exemptions from financial promotion rules and regulations are available, given that the usual exemptions applying to a pure tender offer will not apply (as it is the dealer manager, as intermediary, and not the issuer, who is conducting communications with the issuer's creditors).

Further, investment banking intermediaries which are subject to the "Volcker Rule" under the U.S. Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 will also need to conduct a careful analysis of the extent to which the structure of an intermediated tender or exchange will potentially violate prohibitions on proprietary trading to which they may be subject and, if necessary, to ensure that the transaction is structured in such a way as to access an appropriate exemption (for example, the "market making exemption" where "reasonably expected near term demand of customers" exists).

In addition, should the bonds settled and clear through the ICSDs, the dealer manager will need to assure the ICSDs that it has the issuer's consent to make the offer, otherwise they will not permit it to put out the necessary notices to holders. Similarly, the dealer manager is not strictly bound to put out an SGXNet or HKEx announcement about the tender offer. However, given the overall complicity of the issuer in the transaction structure, it would be advisable to do so on the basis that the issuer has knowledge of the tender offer proceeding and has entered into the exchange settlement agreement which will result in the repurchase and cancellation of the bonds. In addition, the intermediated exchange offer, as a whole, is likely to constitute information which may have a material effect on the price or value of the issuer's debt securities or on an investor's decision whether to trade in such debt securities for the purposes of Rule 745 of the SGX Listing Manual, and may fall within the scope of the announcement requirements under Chapter 37 of the HKEx Listing Rules which apply to debt securities. Equally, considerations surrounding material price sensitive information in the context of market abuse and insider trading are also likely to apply.

4. Specific legal considerations applicable to liability management exercises

Oppression of the minority in exit consents

The decision of the English High Court in the case of *Assenagon Asset Management S.A. and Irish Bank Resolution Corporation Limited (Formerly Anglo Irish Bank Corporation Limited)* [2012] EWHC 2090 (Ch) provides a detailed analysis of the legality of exit consent structures under English law and, in particular, emphasises the position that English courts will not uphold structures that seek to impose unfair or punitive outcomes on dissenting or non-participating bondholders. A detailed analysis of the decision in the *Assenagon* case is the subject of a separate Clifford Chance briefing note, "Liability Management: Exit Consents and Oppression of the Minority", which may be accessed on the Clifford Chance Financial Markets Toolkit¹³, but it is worth summarising the key outcomes thereof insofar as they relate to considerations surrounding the structure of an exit consent:

- Modifications to bond conditions which are *prima facie* detrimental to bondholders may still be within the modification powers forming part of the bond;
- Bonds that have been acquired by an issuer prior to a meeting (at which such modifications are sought to be effected) may be effectively disenfranchised if the terms of the Bonds so provide;
- However, resolutions passed by the majority of bondholders that seek to impose an unfair price or outcome on holders who do not participate in the tender or exchange may be overturned by the courts;
- Open disclosure of the terms of the proposal for the modifications will not save a resolution that is inherently unfair or oppressive to the minority.
- While the facts of the *Assenagon* case reveal a scenario which was overtly oppressive to minority bondholders¹⁴ and therefore relatively easy to assess, other terms proposed for modification may not be as clear-cut, and fall to be carefully considered on a case-by-case basis.

In addition to the common law principles applied to exit consents by the court in *Assenagon*, careful consideration should also be given to the statutory protection afforded to bondholders in different jurisdictions. For example, section 216(b) of the Singapore Companies Act, Chapter 50, provides a statutory remedy to minority bondholders to challenge resolutions in instances where unfair oppression by a majority exists. In the United States, section 316(b) of the U.S. Trust Indenture Act of 1939 effectively prohibits the impairment of a bondholder's right to receive payment of interest and principal without its consent.

Issues of oppression in liability management, and in the context of distressed debt or an insolvency scenario could, depending on the jurisdictions involved, be mitigated through formal court-sanctioned processes such as a scheme of arrangement.¹⁵ Such schemes usually involve a restructuring of all or part of the financial indebtedness of the relevant company, sometimes associated with a related equity restructuring at holding company level, with the existing obligors continuing to conduct the operations of the business. In a successful scheme, the interests of minority dissenting creditors are "crammed down" as a result of the court process,



i.e. as long as the requisite voting thresholds for the scheme proposals are obtained, and the approval of the court is granted, claims of minority dissenting unsecured creditors (such as bondholders) can be compromised without their unanimous consent.¹⁶ As such, a detailed consideration of alternatives should be carried out as part, and at the inception, of a strategic review of any restructuring exercise where concerns such as oppression of the minority might arise.

Voting incentives

It is usual, in the context of consent solicitations, to offer a financial incentive to holders to vote promptly in connection with the extraordinary resolution, often referred to as an “earlybird consent fee”. Sometimes the incentive is available for any vote (either for or against) but often a higher incentive fee is made available only to holders who deliver a vote in favour of the extraordinary resolution on or before a date approximately halfway through the consent process, with no, or a markedly lower, incentive fee payable immediately after such date.

In *Azevedo v Imcopa Importacao and others* [2013] EWCA Civ. 364, the English Court of Appeal considered the legality of such payments in the context of whether they would constitute bribery, and ultimately concluded that such payments would not be unlawful where they are made openly to all bondholders and no bondholders would be prevented from voting.¹⁷ Whilst the decision in *Azevedo* has confirmed that the payment of incentive fees would not invalidate any resolutions taken by a meeting of bondholders, careful consideration needs to be given to the manner in which such fees are structured and paid. In particular:

- It is permissible to provide that incentive fees can be paid only to holders who vote in favour of a resolution; however, it is important to ensure that open disclosure of such fee arrangements is made to all bondholders in the consent solicitation, tender offer or exchange offer memorandum serving as the offering document in the liability management exercise;
- The offer of consent fees to all bondholders will not necessarily cure or otherwise remove concerns of unfair or oppressive conduct (as described above), and will not by itself lead to a conclusion that the proposals are fair; and
- Care should be taken to ensure that any such payments are not routed via the trustee for the bondholders, in order to avoid an argument that the *pari passu* provisions in the trust deed constituting the bonds apply, thereby compelling the trustee to apply the receipt of funds from an issuer in the manner described therein.

In addition, particular care should be taken where a consent solicitation is combined with an exchange offer or tender offer and it is desirable to exclude participation by certain types of investors. As indicated above, while issuers may generally be free to exclude investors in certain jurisdictions which impose onerous requirements, holders can generally not be precluded from participating in a consent solicitation which seeks to modify the terms of a bond. Accordingly, where there are substantial holders in such jurisdictions who are excluded from participating in a tender or exchange offer to which the consent solicitation is allied, it is common to include the concept of a “non-eligible bondholder”, i.e. a bondholder who may not be able to participate in the tender or exchange, but who may nevertheless cast its vote for or against the extraordinary

resolution forming part of the exit consent, and therefore benefit from any incentive fees that may be on offer equally with eligible holders.

Are repurchases specifically permitted under the existing bond terms and conditions?

It is common for bond documentation to contain an express provision permitting the issuer (and any affiliates) to buy back the bonds without restriction. However, it is prudent to check the provisions carefully because, while not common, restrictions on the timing and the manner of buy-backs are not unknown. Also, it is common for bond documentation to specify whether the issuer is obliged to cancel any bonds so purchased or whether it may hold and re-sell any bonds so purchased.

It is also advisable to check whether the rules of the stock exchange or listing authority by which the shares and the bonds are admitted to trading, or applicable laws of the country of that stock exchange or listing authority, provide any restrictions on the timing or manner of buy-backs or offers. In addition, and following amendments made to the SGX Listing Manual on 6 May 2016, an issuer is now required to immediately announce the redemption or cancellation of its debt securities, when every 5 per cent. of the total principal amount of those securities (calculated based on the principal amount at the time of the initial listing) is redeemed and cancelled.¹⁸

Similarly, for consent solicitation exercises, and as noted above (see “Which laws need to be considered? – Governing laws of the trust deed or trust indenture constituting the bonds”), a careful analysis of the terms and conditions of the bonds and the provisions of the trust deed, or indenture, constituting the bonds needs to be undertaken to ensure that the issuer and its advisers are familiar with the matters which require bondholder consent for amendment, and the relevant quorum and voting thresholds necessary to pass such amendments.

Equal treatment of bondholders – tender offers and open market repurchases

The equal treatment of bondholders is usually provided for in the status covenant included in the terms and conditions of the bonds and, in certain jurisdictions, within the listing rules and continuing obligations applicable to bond issues.

Senior-ranking bond issues will typically include a status (or *pari passu*¹⁹) covenant which provides that the bonds will rank without any preference among themselves, and at least *pari passu* with all other unsecured and unsubordinated debt of the issuer.

Under English law, the requirement that the bonds rank without preference among themselves has the effect of being a contractual undertaking by the issuer in favour of bondholders that it will treat all bondholders equally, without favouring certain bondholders over others. As such, and as a contractual matter, an issuer may not repay principal to some, but not other, bondholders (unless otherwise provided for in the terms of the bonds) or otherwise agree to modify the terms of a certain proportion of the bonds.

However, whether this covenant is breached in the context of a tender offer or other bond repurchase which seeks to exclude the participation by certain holders (for example, in the U.S.) requires careful analysis: as a matter of English law, the

requirement that bonds rank ‘without any preference’ seems to restrict preferential treatment in respect of all matters relating to the ownership of the bonds, and is not restricted only to the contractual terms of the bonds.²⁰

It is therefore arguable that an issuer who seeks to exclude the participation of certain bondholders in a tender offer or other bond repurchase exercise is in breach of this covenant where the bond terms do not include an express provision that the issuer (or any of its subsidiaries) may at any time purchase bonds in the open market. Such a buy-back provision is fairly typical in most bond issues governed by English, Singapore or Hong Kong law, however, if no such provision is included, then a partial buy-back may well constitute a breach of the status covenant and the structure of the tender offer should be carefully considered.

From a listing rules perspective, it should also be noted that neither the SGX nor the HKEx has a specific listing rule imposing a requirement for equal treatment similar to that found in the EU Transparency Directive²¹ or as imposed by the UK Financial Conduct Authority.²² However, even if this were the case (and unlike the contractual position above), it is unlikely that a buyback or tender offer would breach an equality of treatment rule, as this would usually only apply to the contractual rights in the bond terms enforceable against the issuer, as opposed to the separate contract formed by the offer to repurchase. That said, the bond terms should be carefully scrutinised to ensure that there is no provision requiring a tender offer to be made available to all bondholders on equal terms: this would have the effect of being a contractual right enforceable against the issuer, and therefore potentially prevent an issuer from excluding the participation of certain bondholders in the tender offer.

“Creeping” tender offers and the risk of integration in open market repurchases

A “creeping” tender offer is one that is generally understood to refer to a series of open market repurchases, privately negotiated in the market (and likely at different prices), which falls short of a full public tender offer made at the same price and equally to all investors. This practice of “creeping” has generally been used as a device to avoid the application of the tender offer rules and, in the Asia-Pacific context, as a way of testing the market’s appetite and gauging appropriate pricing levels prior to making a full-blown public tender offer.

As discussed above (see *“Which laws need to be considered? – United States federal securities laws”*), the U.S. Exchange Act imposes strict requirements on a tender offer for securities that is made to U.S. investors. As such, one of the key risks that exists in relation to open market repurchases (and the practice of creeping) is that one or more negotiated transactions could be deemed to constitute a “tender offer” that does not comply with the U.S. tender offer rules. In this context, a large number of claims brought by disgruntled investors have dealt with open market repurchases that violated the “best price” rule, i.e. where the price offered in the formal tender offer was higher than that which the claimant investor received in its privately negotiated transaction.

While some U.S. courts have applied a strict interpretation and determined that a tender offer starts with the public announcement thereof and ends with its withdrawal or termination, others have taken a more nuanced view in determining whether or not

the open market repurchases (either side of a tender offer) were, in fact, an integral part of the overall tender offer, thereby concluding that the open market repurchases were “integrated” with the formal tender offer, and therefore in violation of the rules prescribed by statute.²³

As such, when a tender offer is contemplated, and will include an offer made to U.S. investors, any open market repurchase activity surrounding the formal tender offer period needs to be carefully considered in light of the risk of integration and, as a general matter, in light of prevailing case law in the U.S., is best avoided.

As described above, liability management transactions that exclude U.S. investors are not subject to the strict requirements of the U.S. rules and, accordingly, any such risk of integration is far lower, given the absence of a statutory or common law obligation (at least outside of the U.S.) on issuers to offer the same price to all investors.²⁴

Nevertheless, other than relevant stock exchange rules that may require an issuer to announce the repurchase of a specified percentage of the outstanding bonds of a series (see *“Which laws need to be considered? – Applicable laws in the issuer’s country and the regulations of the exchange on which the bonds are listed”*, above), issuers and their investment banking advisers should carefully consider issues surrounding open market repurchases conducted in close proximity to a formal tender offer. Although no statutory rights and obligations exist to formally regulate the position, unhappy investors who sold bonds in a privately negotiated transaction concluded immediately prior to a tender offer at a price lower than that offered in the tender offer may still claim damages in tort on the basis that the issuer knew, and failed to disclose, the fact of the following tender offer (and that the investor would have participated in the later offer, had it known of the fact).



Consent solicitations and the “new security” doctrine

From first principles, there is a line of cases in U.S. law where U.S. courts have held that a significant change in the nature of an investment or in the risks attendant on an investment amount to a new investment.²⁵ This has, by extension, been applied by U.S. courts to the amendment of the fundamental economic terms of bonds (such as the rate of interest, principal, maturity, ranking or currency) by way of consent solicitation or meeting of bondholders, to hold that the changes were so central to the basic nature of the bond as to constitute an offering of entirely new securities, with the attendant disclosure obligations that such an offer would impose on issuers.

In the context of recent financial distress scenarios in the Singapore dollar bond market, a common practice has emerged whereby issuers look to amend such fundamental economic terms of their outstanding bonds (for example, the maturity date, interest rate and ranking in the capital structure) by way of a consent solicitation process or meeting of holders, rather than the more traditional techniques associated with substantial amendments to economic terms such as an exchange or tender offer, coupled with exit consent, described above (see “*Liability Management Techniques*”). This approach and development is largely driven by overriding commercial considerations relating to available cash and transaction costs, rather than an assessment of the legal risks involved.

Pursuant to U.S. case law (and U.S. federal securities laws generally), a consent solicitation conducted in those circumstances will carry an amplified risk of being treated as an offering of new securities. There is no reason why courts in common law jurisdictions such as England and Wales, Hong Kong and Singapore would adopt a different view. Accordingly, the absence of any disclosure in those circumstances would bear the risks associated with an offer of securities that does not have the benefit of disclosure and due diligence. In distress scenarios, this could lead to amplified risks for investment banks acting as solicitation agents, as claims for material omissions or misstatements may, as a tactical matter, be directed at them where unsecured bondholders may otherwise have little prospect of recovering their investments from the initial obligors.

As such, proposals to modify the terms of bonds should be carefully considered on a case-by-case basis to determine whether they are likely to constitute an offering of new securities and, even if conducted by way of consent solicitation and bondholder meeting(s), whether additional disclosure should be provided to bondholders in order for them to decide how to vote.

5. Market abuse and insider trading considerations

The Market Abuse Regulation

Directive 2003/6/EC on Market Abuse (the “**Market Abuse Directive**”, or “**MAD**”), was repealed and replaced by Regulation 596/2014 of the European Parliament and of the Council of the European Union (the “**Market Abuse Regulation**”, or “**MAR**”) on 3 July 2016.

Prior to the adoption of MAR, the requirements of MAD only applied to issuers whose debt securities were listed and admitted to trading on regulated markets in the EU, such as the Main Market of the London Stock Exchange. However, one of the key changes brought about by MAR is the extension of the scope of EU market abuse rules to securities that are admitted to trading on EU multi-lateral trading facilities (“**MTFs**”), which includes exchange-regulated markets such as the London Stock Exchange’s Professional Securities Market, the Irish Stock Exchange’s Global Exchange Market and the Luxembourg Stock Exchange’s Euro MTF market.²⁶ In addition, the implementation of the EU Markets in Financial Instruments Directive, or MiFID II, on 2 January 2018, further expands the application of MAR to other organised trading facilities.

While a detailed examination of MAR lies beyond the scope of this work, it will suffice to say that the key obligations that MAR will impose on issuers of debt securities which are admitted to trading on a regulated market or MTF include more stringent requirements surrounding the disclosure of inside information (article 17), the requirement to maintain insider lists (article 18) and the regulation of transactions by persons discharging managerial responsibilities (article 19).

In addition, MAR has a wider scope of application by including securities admitted to trading on an MTF without the issuer’s permission within the ambit of its prohibitions on insider dealing and market manipulation. While the key provisions in articles 17 to



19 will apply only to securities of an issuer who has made an application for, or approved, the admission of its securities to trading on an MTF, the key issue to bear in mind from a liability management perspective is that the universe of potential inadvertent regulatory breaches is now significantly wider under the MAR regime than was the case pre-July 2016, where market abuse considerations were primarily applicable to open market repurchases, and not public liability management exercises such as tender offers and exchange offers.

Further, article 2(4) of MAR effectively provides that the requirements of MAR apply to acts and omissions both within the EU and in third countries (such as Hong Kong and Singapore), and which would be of particular application in the context of the market soundings regime under article 11, where there is a price or value connection to an existing security of the issuer that is trading on an EU regulated market or MTF. Accordingly, particular care should be taken in the execution of liability management exercises conducted for issuers which may have securities which are admitted to trading in the EU or on an MTF, even where the bonds that are the subject of the exercise are not so admitted, but rather are traded on a third country market exchange such as the SGX or HKSE.

Market abuse generally

The analysis in this document assumes that the issuer will be seeking to buy back its bonds for genuine commercial purposes. However, legislative frameworks in certain jurisdictions have led some commentators to suggest that any buy-back of bonds might constitute market abuse, and the adoption of MAR will only serve to increase regulatory risk in any market purchases that an issuer may seek to conduct.

Even where the issuer's motives are beyond reproach, regulators may regard large trading volumes in illiquid markets as securing the price at an abnormal or artificial level. It is therefore important to ensure that the issuer (and any dealer manager acting on its behalf), like any market participant, executes any market purchases in a way which takes into account the need for the market as a whole to operate fairly and efficiently.

These issues are much less likely to arise in relation to properly documented and executed tender offers or exchange offers, in that the prior announcement of the proposed offer and the fact that investors should have equal access to information on the proposed offer should greatly reduce any risk of disorderly markets or other distortions.

Non-public price sensitive information

Different countries are likely to have different tests as to what constitutes non-public price sensitive information or "inside information" but, generally speaking, it can be regarded as information which would, if made public, be likely to have a significant effect on the price of the bonds (and, in the case of convertible bonds, the underlying shares). By way of example, Article 7 of MAR essentially provides that inside information comprises information that is precise, not public, relates directly or indirectly to an issuer or to particular securities, and if made public would be likely to have a significant effect on the price of the securities in question.

For the purposes of this document, it may be helpful to distinguish some different circumstances where information may amount to non-public price sensitive information.

First is the situation where the issuer has information that is unrelated to the proposed buy-back, tender offer or exchange offer, for example information about potential mergers and acquisitions transactions by the issuer. The issuer is unlikely to be able to make market purchases of its own bonds, or launch a tender offer or exchange offer, where it possesses this type of non-public price sensitive information, unless it is prepared to make that information public before making such purchases or offers.

Second is a situation where the proposed buy-back or exchange would itself have a significant effect on the financial condition of the issuer. In the context of a tender offer or exchange offer in these circumstances, the issuer is likely to have to make effective public disclosure of the material facts concerning the offer and its anticipated impact on or before the launch of the offer. For bonds listed on the SGX, Rule 745 of the SGX Listing Manual would apply in this scenario, and the issuer would be required immediately to disclose to the SGX, via SGXNet, any information which may have a material effect on the price or value of its debt securities or on an investor's decision whether to trade in such debt securities. Hong Kong Listing Rule 37.47 would have a similar effect for bonds listed on the HKEx.

If the issuer starts buying its bonds in the market without making any announcement beforehand (because it does not want to be trading at a disadvantage to other market participants), it is likely reasonably quickly to reach a point where its purchases will force it to make a public announcement, either because knowledge of the scale of its purchases will constitute non-public price sensitive information or because the scale of its purchases has been such as to constitute another type of non-public price sensitive information, namely a reduction in the liquidity of the market in the remaining bonds (which would be material to investors' investment decisions). This point is likely to mark the end of the issuer's ability to execute market purchases on comparable terms and, therefore, open market purchases may be less attractive than a tender offer to an issuer wishing to buy back bonds on a significant scale.

Whether the issuer is proposing a tender offer, an exchange offer or a market purchase it will normally be legitimate to delay publication of its intentions, but the issuer must be careful to maintain the confidentiality of its plans and ensure that any disclosure to anyone is only for a legitimate purpose (for example, commercial negotiations with its advisers) and subject to confidentiality undertakings.

Third is a situation where information about the issuer's proposed buy-back would itself have a significant effect on the market for the bonds (or, in the case of convertible bonds, the underlying shares) in the same way as information about a large proposed transaction by any investor. As above, it will normally be legitimate for the issuer to delay publication of its intentions, but the issuer must be careful to maintain the confidentiality of its plans and ensure that any disclosure is only for a legitimate purpose. Also, the fact that the issuer has knowledge of its own intentions to make

market purchases and that such information is price sensitive information generally should not preclude the issuer from carrying out those intentions or a dealer from executing the issuer's orders.

Fourth, as noted above, information that the issuer has executed purchases of its own bonds is likely, once a certain volume of purchases has been effected, to be price sensitive in relation to the remaining bonds, because the reduction in the liquidity of the market in the remaining bonds may be material to investors' investment decisions. This is particularly so where (as is usual) the conditions of the bonds require the issuer to cancel purchased bonds.

Prohibited periods

The rules of the stock exchange or listing authority by which the bonds or any underlying shares are admitted to trading, or the applicable laws of the country of that stock exchange or listing authority, may prescribe certain periods during which the issuer is prohibited from dealing in its own securities or only permit it to do so subject to certain conditions. For example, an issuer which has its primary equity listing on the SGX will generally speaking be unable to launch or execute a tender offer or buy-back in various periods leading up to publication of its regular financial reports.

Tax

An issuer buying back bonds for less than the value of the corresponding liability in its balance sheet is likely thereby to generate income which may be liable to tax. However it may be possible, depending upon the circumstances, to avoid such a liability. An issuer contemplating a buy-back of its bonds would be well-advised to take appropriate tax advice at an early stage.



6. The Accelerated Tender Offer

As highlighted above (see "*Which laws need to be considered? – United States federal securities laws*"), Rule 14e-1 of the U.S. Exchange Act requires that any tender offer be held open for not less than 20 business days from the date the offer is first sent to holders and then held open for an additional 10 business day period from the date any change in the consideration to be paid or the percentage of securities being sought in the offer is sent to holders. Recognising that investors in debt securities are often sophisticated investors and that the decision as to whether to participate in certain basic types of debt tender offers is different from those for equity securities, the SEC staff in 1986 began granting No-Action relief from the 20 day requirement for cash tender offers on investment grade debt.

However, the SEC's Division of Corporation Finance issued a "No-Action Letter" in 2015 which supersedes all prior SEC Staff guidance on accelerated tenders, and has had the effect of creating a category of accelerated tender offers for non-convertible debt securities that can be held open for as little as five business days under the following conditions:

Type of Security

The offer may be made on any class or series of non-convertible debt securities regardless of their rating, including high yield debt securities, and the offer must be made for any and all of such class or series of debt securities.

Who Makes the Offer

The offer must be made by (i) the issuer of the debt securities, (ii) a wholly-owned subsidiary of the issuer, or (iii) a parent company that owns 100% of the issuer.

Tender Offer Consideration

The consideration for the offer can be cash or an exchange for certain "Qualified Debt Securities"²⁷ which are defined as non-convertible debt securities that are identical in all material respects (including the priority of security interests, issuers and/or guarantors, collateral, covenants and other terms) to the subject debt securities except for the changes to the maturity date (which cannot be earlier than the maturity date of the outstanding debt securities), interest payment and record dates, redemption provisions and interest rate (which interest must be payable only in cash).

The consideration offered may be fixed or may be an amount of cash and/or Qualified Debt Securities based on a fixed spread to a benchmark and, in the case of Qualified Debt Securities, the coupon may be based on a spread to a benchmark including U.S. Treasury Rates, LIBOR,²⁸ swap rates and, in the case of securities denominated in currencies other than U.S. dollars, sovereign securities or swap rates denominated in the same currency as the securities subject to the offer, in each case that are readily available on a Bloomberg or similar trading screen or quotation service.

The consideration cannot be financed with the proceeds of any "Senior Indebtedness" which is defined to mean indebtedness that (i) has obligors, guarantors or collateral (or a higher priority with respect to collateral) that the subject debt securities do not have; (ii) has a weighted average life to maturity less than that of the subject debt securities; or (iii) is otherwise senior in right of payment to the subject debt securities; provided that this does not restrict using proceeds from indebtedness or borrowings under any credit or debt facility existing prior to the commencement of the tender offer.

Mechanics of the Offer

The offer must be open to all record and beneficial holders of such class or series of debt securities.

When Qualified Debt Securities are offered as consideration, the exchange offer must be restricted to Qualified Institutional Buyers as defined in Rule 144A (“**QIBs**,”), and/or non-U.S. persons (within the meaning of Regulation S and, collectively with QIBs, “**Eligible Exchange Offer Participants**”) in a transaction exempt from the registration requirements of the U.S. Securities Act. Any holders who are not Eligible Exchange Offer Participants must be given a cash option for their debt securities in a fixed amount determined by the offeror, in its reasonable judgment, to approximate the value of the Qualified Debt Securities being offered.

The offer cannot be made in connection with the solicitation of exit consents or consent solicitations of any kind, and must be announced via a press release through a widely disseminated news or wire service disclosing the basic terms of the offer and containing an active hyperlink to, or an Internet address at which, a record or beneficial holder can obtain copies of the offer to purchase and all other instructions or documents relating to the tender of such debt securities. Such “Immediate Widespread Dissemination” must be made at or prior to 10:00 a.m., Eastern time, on the first business day of the five business day period.

If the issuer or the offeror is a reporting company under the U.S. Exchange Act (including “voluntary filers”), it must furnish the press release announcing the offer in a Form 8-K filed prior to 12:00 noon, Eastern time, on the first business day of the five business day period.

Thereafter, the offeror must communicate any change in the consideration being offered through Immediate Widespread Dissemination and extend the offer for a further five business days (counting the date of such Immediate Widespread Communication as the first business day of the five business day extension); and, if the issuer or offeror is a reporting company, furnish a Form 8-K describing any change in the consideration being offered prior to 12:00 noon, Eastern time, on the first business day of the five business day extension period.

Any other material change to the offer must be communicated through Immediate Widespread Dissemination with the tender offer extended for a further three business days, counting the date of such Immediate Widespread Communication as the first business day of the three business day extension.

The offer must permit tenders prior to expiration through guaranteed delivery procedures, by means of a certification by or on behalf of a holder that such holder is tendering securities beneficially owned by it and that the delivery of such securities will be made no later than the close of business on the second business day after expiration of the offer.

The offer must provide for withdrawal rights that are exercisable (i) at least until the earlier of (x) the expiration date of the offer and (y) in the event that the offer is extended, the 10th business day after commencement, and (ii) at any time after the

60th business day after commencement if for any reason the offer has not been consummated by such day.

The offer cannot include any early payment mechanics but must provide that consideration will not be paid until promptly after expiration of the offer.

Additional Conditions

No abbreviated tender offer can be made:

- if a default or event of default exists under the terms of the subject debt securities or any other indenture or material credit agreement to which the issuer is a party nor if, at the time of the offer, the issuer (i) is the subject of bankruptcy or insolvency proceedings; (ii) has commenced a solicitation of consents for a “pre-packaged” bankruptcy proceeding; or (iii) if the board of directors of the issuer has authorised discussions with creditors of the issuer to effect a consensual restructuring of the issuer’s outstanding indebtedness;
- in anticipation of or in response to, or concurrently with, a change of control or other type of extraordinary transaction involving the issuer, such as a merger (or similar business combination), reorganisation or liquidation or a sale of all or substantially all of its consolidated assets;
- in anticipation of or in response to other tender offers for the issuer’s securities;
- concurrently with a tender offer for any other series of the issuer’s securities made by the issuer if the effect of such offer, if consummated (by way of amendment, exchange or otherwise), would be to add obligors, guarantors or collateral (or increase the priority of liens securing such other series) or shorten the weighted average life to maturity of such other series; or
- within 10 business days after the first public announcement, or the consummation of, the purchase, sale or transfer by the issuer or any of its subsidiaries of a material business or amount of assets that would require the furnishing of pro- forma financial information with respect to such transaction pursuant to Article 11 of Regulation S-X (whether or not the issuer is a registrant under the U.S. Exchange Act).



7. Liability management techniques for sukuk issues

A *sukuk* is defined by the Accounting and Auditing Organisation for Islamic Financial Institutions (the “AAOIFI”) as being “certificates of equal value representing undivided shares in ownership of tangible assets, usufruct and services or (in the ownership of) the assets of particular projects or special investment activity”. Accordingly, while *sukuk* are typically referred to as Islamic bonds (because they essentially replicate the economic features of interest bearing bonds in a *Shari’a* compliant manner), they are better described as an “asset-based investment” as the investors (“*sukuk* holders” or “certificate holders”), own an undivided interest in an underlying asset in proportion to their investment and as such take the risk in, and derive benefit from, the underlying asset. This ownership interest is evidenced by *sukuk* certificates held by the investors, structured as trust certificates.

While a detailed examination of *sukuk* structures lies beyond the scope of this work, in summary, monies raised by the issue of *sukuk* certificates are used to invest in an underlying asset, a trust is declared over that asset as a result of which the certificate holders own a beneficial interest in that asset in proportion to their investment and are entitled to all of the benefits emanating from the asset, including a proportion of the economic returns generated by that asset.

As with all Islamic financial transactions, *sukuk* are based on Islamic principles and jurisprudence (the *Shari’a*) which are derived from a number of sources, including the primary source of the *Qu’ran*. The basic Islamic principle is that money is not a commodity and, therefore, it is not possible to earn profit from its simple utilisation as it has no intrinsic value and is merely a means of exchange. Profit must be earned through trade and taking part in the risks of a transaction.



Accordingly, while all of the considerations highlighted in this work apply equally to liability management exercises relevant to *sukuk*, the underlying asset-based nature of *sukuk* introduces an added layer of complexity that needs to be taken into account when considering a liability management transaction for a series of *sukuk*. To ignore the underlying *Shari’a* principles on which a *sukuk* is based could run the risk of the underlying assets on which the *sukuk* profit return is based no longer being *Shari’a* compliant. In addition, Islamic investors may also require a *fatwa* (i.e. a decision issued by Islamic scholars on the *Shari’a*-compliant nature of the *sukuk*) in relation to the liability management exercise (particularly for exchange offers), where preserving the Islamic-compliant nature of the *sukuk* following the conclusion of the exercise is essential.

Consent solicitations

In relation to conventional debt securities, a consent solicitation can be executed by proposing and soliciting changes to the terms and conditions of the notes (and the underlying trust deed or indenture) through votes of noteholders, and is often accompanied by consent fees aimed at incentivising the participation of investors, which might include an increase in the coupon rate. In distress scenarios, issuers may in turn seek to decrease the coupon rate in order to manage cash flows in times of economic stress.

However, in *sukuk* transactions, any such change in the coupon (usually structured as a periodic distribution of profits based on cash flow generated from the underlying assets) would, in turn, also require an amendment to the underlying asset documentation in order to align the economics of the profit return on the certificates with the profit generated from the underlying assets. If the return is being increased, this may require additional assets being included in the underlying asset structure (for example, additional property in a paradigm *sukuk-al-wakala* sale and leaseback structure).

Tender offers

Using a paradigm *sukuk-al-ijara* structure as an example, the underlying obligor (i.e. the ultimate credit) sells physical assets to an SPV issuer (which also declares a trust over those assets in favour of the investors) which is financed by cash raised from the sale of the *sukuk* to investors. The SPV issuer then leases the assets back to the obligor, with the lease rental payments from the obligor then mirroring the periodic distribution payments (i.e. the equivalent of the coupon) made to investors, thereby servicing those payments.

Accordingly, if the obligor were looking to conduct a cash tender offer for the *sukuk* in future, it would be important to ensure that some relationship exists between the SPV issuer and the obligor, in order to allow the obligor to repurchase some or all of the *sukuk* that are the subject of the tender, and to then effectively collapse the trust and unwind the contractual arrangements between the SPV issuer and the obligor.

While tender offers are arguably less complex in an Islamic finance context (given the cash nature of the transaction and the likelihood that the *Shari’a* compliant nature of the *sukuk* need not be maintained if they are to be repurchased and cancelled), careful consideration should be paid to the ability of the obligor and SPV issuer to unwind the

structure: in this respect, an optimal approach could be for the SPV issuer to conduct the tender offer, with a corresponding amount of assets purchased from the obligor and the trust over the assets (or proportion of the assets corresponding to the *sukuk* accepted for repurchase) dissolved under the terms of the declaration of trust and other asset documentation constituting the *sukuk*.

Exchange offers

An exchange offer of *sukuk*, particularly where one series of *Shari'a*-compliant trust obligations is to replace another series of *Shari'a*-compliant trust obligations, is likely the most complex liability management exercise in light of the underlying asset structure and the probable need to maintain *Shari'a* compliance of the new securities (which will likely also require a *fatwa* from Islamic scholars).

Given that the original SPV issuer will typically covenant in favour of certificate holders not to undertake any activities outside of the context of the original *sukuk* issuance (a feature common to all *sukuk* offerings), it is probable that the SPV will, by the terms of the *sukuk*, be prohibited from conducting an exchange offer. Similarly to tender offers, there will also need to be some nexus between the issuer SPV and the obligor which will allow the exchange offer to be consummated in a manner that preserves the underlying economics and cash flows of the assets on which the *sukuk* is based and, in turn, the *Shari'a* compliant nature of the *sukuk*.

To achieve this, a potential approach would be to establish a second SPV as the issuer of the new *sukuk* to be offered in the exchange which, in turn, would need to be collateralised by an asset base with similar economic and cash flow features. In addition, a contractual mechanism would also need to be put in place to extinguish the obligor's obligations under the original series of *sukuk* and replacing them with the corresponding obligations under the new series.

As with liability management exercises for conventional debt securities, the contractual technology of a consent solicitation, tender offer and exchange offer can be combined in an optimal manner in order to meet the specific objectives of the obligor but, as briefly summarised above, the underlying contractual arrangements will need to be considered in the structuring of the transaction if the *Shari'a*-compliant nature of the transaction is not to be compromised.

Conclusion

Depending upon the circumstances, liability management exercises can offer significant economic benefits to issuers, both as a form of pro-active balance sheet liability management and in a broader distressed debt or restructuring scenario. However, the variety of different techniques and the potential for various laws and regulatory regimes to impact the process mean that an issuer should not embark upon a liability management exercise without first giving careful consideration to the issues described in this document.

References

- Exchange Release, No. 34-30967, 28 July 1992.
- Abbreviated Tender or Exchange Offers for Non-Convertible Debt Securities, SEC No Action Letter (23 January 2015).
- Rule 323, Part VII (Continuing Listing Obligations), SGX Listing Manual.
- Rule 324(1), Part VII (Continuing Listing Obligations), SGX Listing Manual.
- Rule 37.47, HKEx Listing Rules.
- Rule 37.48, HKEx Listing Rules.
- Rule 37.49(a)-(b), HKEx Listing Rules.
- However, following a market consultation process in 2012 concerning tender offer regulations, CONSOB (the Italian securities regulator) has approved new secondary regulations which aim to simplify the procedure applicable to tender and exchange offers for debt securities, as well as to reduce the costs and the administrative burden of these transactions and ensure that rules on offers for debt securities are consistent with European practice. This is the subject of a separate Clifford Chance briefing note, "Liability management: green light in Italy", accessible on the Clifford Chance Financial Markets Toolkit: <http://financialmarketstoolkit.cliffordchance.com>
- An acronym used by the ICSDs for the advance notice of "Deadlines and Corporate Events."
- I.e. an "invitation memorandum", "offer to purchase" or "tender offer memorandum" in the case of tender offers; an "exchange offer memorandum" in the case of an exchange offer; and a "consent solicitation statement" in the case of a consent solicitation.
- In the case of CDP, the blocking is effected by CDP once the holder of record manually submits its instruction which, in turn, needs to be manually supported by the agent.
- For example, the need to announce repurchases or redemptions when certain thresholds are met, as discussed under "*Which laws need to be considered? – Applicable laws in the issuer's country and the regulations of the exchange on which the bonds are listed*", above.
- Clifford Chance Financial Markets Toolkit: <http://financialmarketstoolkit.cliffordchance.com>
- In that case, the resolution proposed as part of the exit consent had the effect of including a call option in the bond documentation which would allow Irish Bank, as the issuer, to redeem all bonds not tendered for exchanged for EUR0.001 per EUR1,000 in principal amount of the outstanding bonds.
- A scheme of arrangement is typically a court-supervised process (in the United Kingdom, under the Companies Act 2006), which aims to implement an agreement between a debtor and its creditors. Regardless of the jurisdiction of incorporation of the issuer, an English court has jurisdiction to sanction a scheme of arrangement in a company that has a "sufficient connection" to England. A "sufficient connection" is usually established by the "Centre of Main Interests" of the company, or the governing law and jurisdiction clauses in its underlying finance documents. Accordingly, a company incorporated outside of England may be able to use a scheme of arrangement under the English Companies Act 2006 where the terms and conditions of its bonds, and the trust deed constituting its bond issue, is expressed to be governed by English law.
- Such a "cram down" scheme distinguishes a scheme of arrangement from a company voluntary arrangement which does not bind secured creditors. Accordingly, where bonds are secured, this alternative may not be commercially or practically feasible.
- A detailed analysis of the decision in the *Azevedo* case is the subject of two separate Clifford Chance briefing notes ("*Noteholder Meetings: Paying the Price for Change*" and "*Consent Fees and Noteholder Meetings*", which may be accessed on the Clifford Chance Financial Markets Toolkit: <http://financialmarketstoolkit.cliffordchance.com>).
- Rule 324(1), Part VII (Continuing Listing Obligations), SGX Listing Manual, which replaced Rule 747(1) which used to require an issuer to specifically announce, via SGXNet, any cancellation or redemption of its debt securities.
- Meaning, literally, 'side by side' or 'in equal step'.
- See Geoffrey Fuller, *The Law and Practice of International Capital Markets*, 3rd Ed., at 9.16.
- 2004.109/EC, Article 18.1.
- Disclosure and Transparency Rules, Rule 6.1.3(2).
- See, for example, *Field v Trump*, 850 F.2d 983 (2nd Cir. 1988).
- This is assuming that the terms and conditions of the bonds do not, as a contractual matter, impose an obligation on the issuer to make any "tender offer" or other buy-back available at the same price to all investors, in which case, the same risks will apply regardless of the jurisdiction in which the offer is made.
- See, for example, *Keys v Wolfe*, 709 F.2d 413 (5th Cir. 1983).
- These exchange-regulated markets were traditionally popular with issuers as they fell outside of the remit of the EU Prospectus and Transparency Directives, meaning that there were less onerous obligations imposed on issuers both at the time of the initial listing, as well as in respect of continuing obligations.
- The concept of "Qualified Debt Securities" is not to be confused with "Qualifying Debt Securities" under the Singapore QDS Scheme.
- References to LIBOR in the 2015 No-Action Letter should be considered against the backdrop of the market shift away from LIBOR and towards alternative benchmark rates.

CONTACTS

Greater China



Connie Heng
Partner, Head of
Capital Markets APAC
T: +852 2826 2457
E: connie.heng@
cliffordchance.com



Matt Fairclough
Partner
T: +44 20 7006 1717
E: matt.fairclough@
cliffordchance.com



Alexander Lloyd
Foreign Legal
Consultant
T: +852 2826 3447
E: alexander.lyod@
cliffordchance.com



Angela Chan
Partner
T: +852 2825 8891
E: angela.chan@
cliffordchance.com

Singapore



Johannes Juette
Partner
T: +65 6410 2293
E: johannes.juette@
cliffordchance.com



Raymond Tong
Partner
T: +65 6410 2253
E: raymond.tong@
cliffordchance.com



Rahul Guptan
Partner
T: +65 6410 2295
E: rahul.guptan@
cliffordchance.com



Gareth Deiner
Partner
T: +65 6410 2202
E: gareth.deiner@
cliffordchance.com



David Tsai
Partner
T: +852 2826 2466
E: david.tsai@
cliffordchance.com



Fang Liu
Partner
T: +852 2825 8919
E: fang.liu@
cliffordchance.com



Jean Thio
Partner
T: +65 6506 1956
E: jean.thio@
cliffordchance.com



Mark Chan
Partner
T: +852 2826 3424
E: mark.chan@
cliffordchance.com

Seoul



Richard Lee
Partner
T: +852 2825 8911
E: richard.lee@
cliffordchance.com



Leng-Fong Lai
Co-Managing Partner
T: +813 6632 6625
E: leng-fong lai@
cliffordchance.com



Reiko Sakimura
Co-Managing Partner
T: +813 6633 6616
E: reiko.sakimura@
cliffordchance.com



Scott Bache
Partner
T: +852 2826 3493
E: scott.bache@
cliffordchance.com



James Booth
Senior Consultant –
Head of Corporate
Trusts(AP)
T: +852 2826 2430
E: james.booth@
cliffordchance.com

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London, E14 5JJ

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