

Insights

THE TAKEOVER PANEL PUBLISHES CHANGES TO RULE 21 (RESTRICTIONS ON FRUSTRATING ACTION)

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SUMMARY

Following on from its earlier consultation, the Code Committee of the Takeover Panel has published its amendments to Rule 21 of the Code which take effect on 11 December 2023 and apply to on-going transactions which straddle this date.

The principal changes amend Rule 21.1 so that the board of a target company would no longer be restricted from taking an action that either is not material or is in the ordinary course of its business and which would not result in an offer or bona fide possible offer being frustrated. The aim of the changes are to increase flexibility for target companies to carry on their ordinary course activities, including where these involve buying and selling assets, and to provide greater clarity as to the action that will and will not be restricted.

Separately the Panel Executive has published changes to Practice Statement No. 5 (Rule 13.5 – invoking conditions and pre-conditions).

RESTRICTIONS ON ACTIONS BY THE BOARD OF THE TARGET COMPANY

Rule 21 of the Code currently restricts a target board from taking certain actions without shareholder approval, on the basis that those actions might result in an offer or a possible offer being frustrated. Although the provisions, for the most part, operate satisfactorily, the restrictions have not been changed for a number of years and are no longer proportionate given the lengthy timetables involved in takeover offers these days.

Going forward, issuing shares or convertible securities, granting options or share awards and redeeming or purchasing its own shares will be 'restricted actions' unless in the ordinary course of target's business. This means that a proposed issue of new shares in the ordinary course of target's business would be permitted but any other issue of new shares would be a restricted action, even if

not material, and would require Panel consent or shareholder approval. The Panel has identified that in relation to an issue of shares as consideration for an acquisition it will consider the following matters when determining whether the issue is in the ordinary course of target's business and therefore permissible:

- the frequency with which target has issued shares or convertible securities as consideration for an acquisition of assets;
- the size and terms of the proposed issue; and
- whether the acquisition itself would be in the ordinary course of target's business.

EMPLOYEE INCENTIVISATION ARRANGEMENTS

The Panel have also identified that it would not be unusual for target boards to seek to grant options over, or awards in respect of, shares to the target company's employees under existing employee share incentive schemes during a restricted period and has confirmed that such actions will be considered ordinary course and not normally restricted.

Similarly, the Panel has confirmed that Rule 21.1 should not normally prevent a grant of options or awards in respect of shares in connection with a new appointment, promotion or hire if it is:

- in accordance with normal practice under an established incentive scheme; or
- if it is consistent with the target's proposed practice under a new incentive scheme and it was publicly disclosed before the relevant period, for example in a prospectus or a shareholder circular.

PERIOD RESTRICTIONS WILL APPLY

The restrictions will apply from the earlier of: (i) an approach by a potential bidder to the target board and (ii) the beginning of the offer period, and ending at the end of the offer period or 5pm on the seventh day after the proposed offer is rejected by the board. Previously this was two business days but this is considered too short a window for a rejected potential bidder to make a further approach.

APPLICATION OF THE RULE TO A REVERSE TAKEOVER

Rule 21.1 will also apply during the relevant period to the board of the bidder where an offer is a reverse takeover.

New [Practice Statement No 34](#) (Appendix C) provides additional guidance on how the Panel interprets and applies Rule 21.1 and minor amendments have also been made to Practice

Statement No 2, Practice Statement No 29, Practice Statement No 30 and Practice Statement No 31.

CHANGES TO PRACTICE STATEMENT NO. 5 (RULE 13.5 - INVOKING CONDITIONS AND PRE-CONDITIONS)

Practice Statement No 5 (PS5) describes the way in which the Panel Executive interprets and applies Rule 13.5 when a bidder may invoke a condition or pre-condition to an offer so as to cause an offer to lapse, be withdrawn or not proceed. Rule 13.5(a) requires an overriding standard of materiality to be satisfied before a bidder can invoke a condition.

The changes to **PS 5** include:

- splitting the conditions in a typical offer into six broad categories including a new condition in relation to long-stop dates and so-called “mini-long-stop dates”. Previously they were broken down into four broad categories;
- guidance clarifying that certain types of conditions may not be subject to Rule 13.5(a) circumstances. For example, a condition relating to the approval by target company shareholders of a transaction or a condition relating to an action by shareholders in the target company such as the rejection of an acquisition or disposal proposed by the target board;
- the factors the Panel will take into account when considering whether the ‘material significance’ requirement has been satisfied including the actions taken by the bidder since the firm offer announcement. For example, if the bidder has purchased shares in the target company, since the relevant circumstances arose, or has made statements indicating an intention to continue to pursue the bid, the Panel will be less supportive of invocation. Also, if the target board agrees with an invocation request by the bidder, the Panel is more likely to agree to this;
- the Panel taking into account management time, costs and other burdens when considering whether the material significance requirement has been satisfied in relation to a Phase 2 reference condition; and
- clarification that if on a long-stop date a review by a regulatory body in relation to a material official authorisation or regulatory clearance has not concluded, the bidder will normally be able to lapse its offer.

These changes to PS5 come into effect immediately.

RELATED PRACTICE AREAS

- M&A & Corporate Finance
- Securities & Corporate Governance
- UK Public Company

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