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There is cause for optimism and caution in light of the past year’s events.

First, we can be tentatively optimistic about Europe. The possibility of a euro breakup appears to have faded, and European equities markets performed, on the whole, exceptionally well in 2013. Indeed, the euro/dollar basis swap has moved sufficiently to open up euro capital markets to borrowers wishing to swap proceeds to dollars; the World Bank sold its first euro benchmark bond for more than four years in November 2013, and non-European companies like Sinopec and Korea Natural Gas have issued large euro bonds in recent months. If the European economy continues to grow (and analysts are expecting growth to quicken), it is hoped that the prospect of crisis will continue to fade.

Second, though 2013 was a comparatively languid year for global M&A, the buoyancy of the credit and equity markets cannot be ignored. In terms of financing, the seeming willingness of banks to allow for looser borrower constraints, to underwrite jumbo facilities in small syndicates, and to offer flexible and fast bridge-financing for high-value acquisitions, presents a financing climate that should be particularly amenable to corporate M&A. It is also notable that continued political and economic instability did not impede the completion of some standout deals in 2013, including the Glencore/Xstrata tie-up and Vodafone’s disposal of its shareholding in Verizon Wireless. These deals show that market participants are able, for the right deal, to pull out all the stops. After a period of introspection and careful balance sheet management, corporates may be increasingly tempted to put cash to work through M&A.

There remains, however, cause for prudence. There is considerable uncertainty as to how markets will process the tapering of quantitative easing (QE) by the US Federal Reserve. The merest half-mention by Ben Bernanke, in May 2013, of a possible end to QE was enough to shake the markets, and to nearly double the 10-year US Treasury yield in a matter of months. Emerging markets are particularly sensitive to these shocks. The oncoming end of QE may already have been priced into the markets, but there is a possibility that its occurrence will cause further, severe market disruption. In addition, there are concerns around how the funding gap left by huge bank deleveraging will be
filled, and centrifugal pressures continue to trouble European legislators. Finally, there are broader concerns as to the depth of the global economic recovery as growth in the BRIC economies seems to slow. Optimism should, therefore, be tempered with caution.

I would like to thank the contributors for their support in producing the eighth edition of The Mergers & Acquisitions Review. I hope that the commentary in the following chapters will provide a richer understanding of the shape of the global markets, together with the challenges and opportunities facing market participants.

Mark Zerdin
Slaughter and May
London
August 2014
Chapter 67

UNITED KINGDOM

Mark Zerdin

I OVERVIEW OF M&A ACTIVITY

In a languid year for M&A activity in Europe and globally, the United Kingdom remained substantially the liveliest market for dealmaking in Europe. Of European M&A activity in 2013, the UK accounted for 19.9 per cent of transactions by volume (some 1,104 deals). Perhaps more notably, for the year as a whole the UK was second only to the United States as both a destination for acquirers and as a source of outbound acquirers. In absolute terms, however, 2013 was still a lacklustre year for M&A in the UK and globally, with the value of global deals depressed by 14 per cent relative to 2012 (a total value of US$1,827 billion), and a volume of deals that was the lowest since 2009 (2,263). Public M&A activity in the UK was substantially reduced relative to 2012: only nine firm offers were made for Main Market companies in 2013, versus 24 in 2012. Deal values were also notably depressed: of the 39 firm offers made for Main Market and AIM listed companies reviewed by PLC’s ‘What’s Market’, 13 had a value of over £100 million, and only three had a value exceeding £1 billion (versus 21 and eight respectively for 2012).

There were, however, some standout UK transactions in 2013. Liberty Global’s acquisition of Virgin Media for roughly £14.9 billion in a mix of cash and shares was the year’s sole UK mega-deal. The acquisition was part-financed by a large high-yield

1 Mark Zerdin is a partner at Slaughter and May. The author would like to thank Will Manley for his assistance in preparing this chapter.
3 Allen & Overy LLP, M&A Index, Q4 2013, pp. 8–9.
4 Ibid., p. 5.
bond issue by Liberty Global, reminiscent of the mid-2000s style junk issuances which financed much of M&A prior to the financial crisis. This was the first in a string of major UK and European telecommunications transactions which has continued into 2014, and includes Vodafone Group plc’s acquisitions of Kabel Deutschland Holding AG for approximately £6.6 billion and Grupo Corporativo ONO SA for €7.2 billion. The UK, with a very strong TMT sector, is exceptionally well-placed to take advantage of a TMT market which is at its liveliest since 2007. The UK also remained in 2013 a highly attractive market for inward M&A investment, with 86 deals involving overseas acquirers (second only to the US). Of the firm offers announced for Main Market or AIM listed companies in 2013, 62 per cent involved a non-UK bidder. Non-UK bidders were also responsible for the highest value bids. French group Schneider Electric SA, for instance, acquired Invensys plc for £3.4 billion in a mix of cash and shares and, in what would have been one of the year’s highest value deals had it gone ahead, a consortium comprising Borealis Infrastructure Management Inc, the Kuwait Investment Office and Universities Superannuation Scheme Limited submitted a pre-conditional cash proposal of over £5 billion to the board of Severn Trent plc. The proposal, however, was rejected.

There was a more even divide between schemes of arrangement and contractual offers in 2013, reports PLC’s ‘What’s Market’, but the bare numbers are misleading. Of the firm offers announced for Main Market companies in 2013, four were announced as schemes and five as contractual offers. Of the contractual offers, however, one was not recommended by the independent committee of the target board, two were mandatory offers, and another was originally hostile and latterly mandatory. Two of the contractual offers also involved a US tender offer. Of the four firm offers announced as schemes, three had a value in excess of £100 million. Of the 30 firm offers announced for AIM companies in 2013, there was an even split between schemes and contractual offers but, again, the majority of offers with a value in excess of £50 million were structured as schemes. It would appear, therefore, that the scheme structure continues to be preferred for high value recommended bids.

The effect of China’s relatively new merger control regime may also be beginning to creep into UK dealmaking. Global filings with MOFCOM’s Anti-Monopoly Bureau are estimated to have risen to some 200 in 2013, with almost half of those filings concerning foreign-to-foreign transactions. MOFCOM appears to be growing increasingly aggressive in its application of Chinese antitrust rules. It was Chinese antitrust approval which delayed completion of the enormous Glencore/Xtrata merger of May 2013, and it was Chinese approval which also unexpectedly stalled Dentsu Inc’s acquisition of London-listed Aegis for a period of several months. In what may become a standard feature of sizeable M&A transactions, Schneider Electric’s offer for Invensys was subject to a condition that MOFCOM indicated, in terms reasonably satisfactory to Schneider, that it did not intend to conduct further review under the relevant article of

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6 Allen & Overy LLP, ibid.
7 PLC, ibid. p. 20.
8 PLC, ibid. p. 4.
China’s antitrust legislation, such was Schneider’s concern as to MOFCOM’s continuing surveillance. Other antitrust regulators stymied a number of deals in 2013, chiefly a proposed tie-up of Britvic and AG Barr which, although all but agreed in November 2012, slowly collapsed following referral by the Office of Fair Trading to the EU Competition Commission (even though clearance was ultimately granted by the regulator).

One of the factors possibly inhibiting the M&A market has been a pronounced move toward IPOs as an exit for private equity firms. A string of well-known retail names have been guided by private equity houses to extremely successful flotations in recent months, including Pets At Home (formerly majority owned by KKR) and Poundland (a prior asset of Warburg Pincus). Companies including Made.com and B&M are also apparently mulling flotations. There is a risk that the quality of these listings will deteriorate. Recent flotations, including that of Saga, priced at the lower end of the range, and the retailer Fat Face decided to pull their planned listing at the last minute, citing a lack of interest. There is a possibility that, after such a rush of activity, the IPO market will show increasing discipline.

If 2013 was a year of considerable promise but languid activity, the start of 2014 has seen a rush of bulge-bracket deals which could signal a much anticipated return to high-value M&A. In the four months to the end of April 2014, there were 15 transactions each worth more than US$10 billion, the most since the record year of 2007.10 Of these, two examples involve UK companies; GlaxoSmithKline’s three-pronged purchase, sale and joint venture deal with Novartis (to the value of US$16 billion), and Pfizer’s frustrated bid for AstraZeneca, which valued the UK pharmaceuticals manufacturer at £69.4 billion. These sorts of transactions strongly suggest an increased investor and boardroom confidence in the prospects of the UK and global economy.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

The Companies Act 2006 (the 2006 Act) provides the fundamental statutory framework and, together with the law of contract, forms the legal basis for the purchase and sale of corporate entities in the UK. In addition, the City Code on Takeovers and Mergers (the Takeover Code, or the Code) regulates takeovers and mergers of certain companies in the United Kingdom, the Isle of Man and the Channel Islands. The Takeover Code has statutory force, and the Takeover Panel has statutory powers in respect of the transactions to which the Takeover Code applies. Breach of any of the Takeover Code rules that relate to the consideration offered for a target company could lead to the offending party being ordered to compensate any shareholders who have suffered loss as a consequence of the breach. In addition, breach of the content requirements of offer documents and response documents may constitute a criminal offence. The Panel also has the authority to issue rulings compelling parties who are in breach of the requirements of the Takeover Code to comply with its provisions, or to remedy the breach. These rulings are enforceable by the court under Section 955(1) of the 2006 Act. The Code has a wider scope than the

10  The Economist, ‘Return of the big deal’, 8 May 2014.
EU Takeovers Directive, and applies if the offeree (or potential offeree) is a UK public company and in some instances if the company is private or is dual-listed.

The Financial Services and Markets Act 2000 (FSMA) regulates the financial services industry and makes provision for the official listing of securities, public offers of securities and the communication of invitations or inducements to engage in securities transactions. Following the substantial amendments to the FSMA, brought about on 1 April 2013 when the Financial Services Act 2012 (the FS Act) came into force, financial regulation in the UK is split between two new bodies: the Financial Conduct Authority (FCA), which regulates conduct in retail and wholesale markets, and the Prudential Regulation Authority (PRA), which is responsible for the prudential regulation of banks and other systemically important institutions. As a consequence of the FS Act, over 1,000 institutions (including banks, building societies, credit unions and insurers) are now ‘dual-regulated’. The FSMA also established a regime to prevent market abuse. The UK Listing Authority Sourcebook of Rules and Guidance (which includes the Listing Rules, the Prospectus Rules, and the Disclosure and Transparency Rules (DTRs)), promulgated by the FCA in its capacity as the UK Listing Authority (the competent authority for the purposes of Part VI of the FSMA), includes various obligations applicable to business combinations involving listed companies and contains rules governing prospectuses needed for public offers by both listed and unlisted companies. The Listing Rules, in particular, set out minimum requirements for the admission for the admission of securities to listing, the content requirements of listing particulars, and ongoing obligations of issuers after admission. The Criminal Justice Act 1993, together with the Listing Rules, the DTRs and the Takeover Code, regulate insider dealing.

The merger control rules of the United Kingdom are contained in the Enterprise Act 2002, although the rules do not generally apply to mergers in relation to which the European Commission has exclusive jurisdiction under the EU Merger Regulation. In addition, specific statutory regimes apply to certain areas, including water supply, newspapers, broadcasting, financial stability, telecommunications and utilities, and these separate regimes may have practical implications in merger situations.

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

There have been several recent developments in respect of the Takeover Code and the Listing Rules which have served to clarify, to a certain extent, areas of ongoing ambiguity or uncertainty.

i The FCA’s new listing regime
In November 2013, the FCA issued consultation paper CP13/15, which included a package of measures designed to strengthen minority shareholder rights and protections where they are at risk of being abused. The proposed measures were particularly intended to deal with instances where a controlling shareholder does not maintain an appropriate relationship with a premium listed company.

On 16 May 2014 the FCA published Policy Statement PS14/8. This followed the publication of the Listing Rules (Listing Regime Enhancements) Instrument 2014
(FCA 2014/33) which has amended the FCA Handbook with effect from 16 May 2014. The Instrument implements the amendments proposed in CP 13/15 in substantially the form in which they were proposed. Key amendments are as follows:

a A premium listed company with a ‘controlling shareholder’ (that is, any person who exercises or controls on their own or with any person with whom they are acting in concert, 30 per cent or more of the company’s voting rights) is now required to enter into a written and legally binding agreement with that controlling shareholder. Such an agreement, the FCA intends, will contain mandatory independence provisions that are fundamental to the ability of the company to operate as an independent business, and the existence of such an agreement must be disclosed in the company’s annual report.

b A dual voting structure for the appointment of independent directors of a premium listed company with a controlling shareholder has been introduced. Under this new system, appointments will need to be approved both by the shareholders as a whole and by the ‘independent shareholders’ (that is, all holders of shares except the controlling shareholder).

c A requirement for additional approval by independent shareholders has been introduced in respect of the cancellation of a premium listed company’s listing. For a cancellation to be approved, a premium listed company must now obtain approval from at least 75 per cent of voting rights attaching to all shares voted on the resolution and, in addition, a simple majority of the votes attaching to shares of independent shareholders voted on the resolution.

d Under the Listing Rules, a controlling shareholder and its associates must not propose (or procure the proposal) of a shareholder resolution which is intended to circumvent the proper application of the Listing Rules. The FCA has stated that this is not intended to unduly restrict a shareholder from fairly engaging in company matters, but chiefly to reinforce the new cancellation of listing provisions.

One issue on which the FCA declined to offer guidance was its interpretation of the term ‘acting in concert’. The FCA does not wish to restrict either its or the Takeover Panel’s discretion on this point, but some recent guidance on this term has been issued by the European Securities and Markets Association (ESMA), and is detailed below.

ii ESMA issues guidance on acting in concert

The Takeover Directive (2004/25/EC) was subject to a review by the Commission which was published in June 2012. One of the major recommendations of the review was for there to be greater clarity around shareholder cooperation and ‘acting in concert’, both concepts having been subject to considerable ambiguity since the Directive was introduced. If multiple shareholders in a company are deemed to be ‘acting in concert’ with each other in respect of that company, the cooperating shareholders may be treated as a single entity for the purposes of the Directive and the UK Takeover Code and may, if their aggregate shareholding surpasses a specified threshold, be required to make a mandatory bid for the company as a whole. Investors have therefore voiced concern that this risk inhibits them from cooperating on corporate governance matters.
On 12 November 2013 ESMA published a statement addressing the issue. The statement includes a ‘White List’ setting out a number of activities which, if practised by cooperating shareholders, will not be subject to a presumption that the shareholders are acting in concert. These activities are as follows:

\( a \) Entering into discussions with each other about possible matters to be raised with the company’s board;

\( b \) making representations to the company’s board about company policies, practices or particular actions that the company might consider taking;

\( c \) other than in relation to the appointment of board members, exercising shareholders’ statutory rights to (1) add items to the agenda of a general meeting; (2) table draft resolutions for items included or to be included on the agenda of a general meeting; or (3) call a general meeting other than the annual general meeting; and

\( d \) other than in relation to a resolution for the appointment of board members and insofar as such a resolution is provided for under national company law, agreeing to vote the same way on a particular resolution put to a general meeting, in order to, for example, reject a related-party transaction, or to approve or reject:

- a proposal relating to directors’ remuneration;
- an acquisition or disposal of assets;
- a reduction of capital and/or share buy-back;
- a capital increase;
- a dividend distribution;
- the appointment, removal or remuneration of auditors;
- the appointment of a special investigator;
- the company’s accounts; or
- the company’s policy in relation to the environment or any other matter relating to social responsibility or compliance with recognised standards or codes of conduct.

The statement makes clear that engaging in an activity that is not included in the White List will not, in and of itself, mean that the cooperating shareholders will be deemed to be acting in concert; each instance is to be considered on its own facts, and shareholders are encouraged to consult with the relevant national competent authority for guidance.

It is notable, however, that the White List does not include any activity relating to cooperation in relation to board appointments. This is in deference to the company law of respective Member States, but the statement does provide that such cooperation may take the form of:

\( a \) entering into an agreement or arrangement (informal or formal) to exercise their votes in the same way in order to support the appointment of one or more board members;

\( b \) tabling a resolution to remove one or more board members and replace them with one or more new board members; or

\( c \) tabling a resolution to appoint one or more additional board members.

In considering cooperation in relation to board appointments, ESMA expects national competent authorities to examine, \textit{inter alia}, the nature of the relationship between
the shareholders and the proposed board member(s), the relationship between the shareholders, their objectives and their actions or the result of their actions, whether the shareholders have cooperated in relation to the appointment of board members on more than one occasion, and whether the appointment of the proposed board member(s) will lead to a shift in the balance of power on the board.

iii Takeover Panel issues Practice Statement on Directors’ Irrevocable Commitments and Letters of Intent

Under Rule 21.2(a) of the Takeover Code, neither the offeree company nor any person acting in concert with it may, except with the Panel’s consent, enter into any offer-related arrangement with the offeror or any person acting in concert with the offeror during an offer period or when an offer is reasonably in contemplation. On 17 January 2014, the Panel issued Practice Statement No. 27 clarifying its interpretation of Rule 21.2 and its relation to irrevocable commitments and letters of intent given by offeree shareholders who are also directors of the offeree company. The Panel has confirmed that irrevocable commitments and letters of intent fall outside the ambit of ‘offer-related arrangements’ and are therefore permissible. However, although Rule 21.2 permits a shareholder-director to make an irrevocable commitment or give a letter of intent to accept an offer, it does not allow such person to make other offer-related commitments favourable to the offeror, for example:

a not to solicit competing offers;
b to recommend an offer to offeree company shareholders;
c to notify the offeror if the director becomes aware of a potential competing offer;
d to convene board meetings and/or vote in favour of board resolutions that are necessary to implement the offer;
e to provide information in relation to the offeree company for due diligence or other purposes;
f to assist the offeror with the satisfaction of its offer conditions;
g to assist the offeror with the preparation of its offer documentation; and
h to conduct the offeree company’s business in a particular manner during the offer period.

This statement serves to further narrow the legal scope of irrevocable commitments and letters of intent, and is consistent with one of the Code’s overarching purposes; to, as far as possible, provide for equality among rival offerors.

IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

In a record year for foreign direct investment (FDI) into Europe, the UK remained the leading market for foreign investors. Ernst & Young reports, in its European Attractiveness Survey 2014, that there were a record 799 FDI projects in the UK in 2013, representing
a 20 per cent share of the European total.\textsuperscript{11} The UK also ranked foremost in terms of FDI job creation, and as the largest recipient of FDI R&D projects, with a 22 per cent share of the European market. The UK and Germany collectively comprised fully 38 per cent of all FDI projects in Europe in 2013, as foreign investors jostled to acquire a presence in two of the continent’s largest and wealthiest markets. It would appear, indeed, that (as forecast by Ernst & Young in their UK Attractiveness Survey 2013) Germany is fast approaching parity with the UK as a European destination for foreign investors.

Globally, the UK was second only to the US as a destination for foreign acquirers; 86 transactions involving foreign acquirers were completed in 2013, to the value of US$72.5 billion.\textsuperscript{12} Of the firm offers announced in 2013 for Main Market or AIM listed UK targets, 62 per cent involved a non-UK bidder, reports PLC’s ‘What’s Market’.\textsuperscript{13} The US was foremost among foreign acquirers investing in the UK; 40 deals involved US acquirers, to the value of US$36.3 billion. Behind the US came France, Germany and Japan (whose UK spend was swollen by Dentsu’s £3.2 billion acquisition of Aegis). Canadian buyers also made five UK acquisitions, to a total value of US$3.3 billion.

It should be noted, however, that the total value of acquisitions of UK companies by foreign buyers for 2013, enormously bloated as it was by the Glencore/Xstrata tie-up, rather artificially flatters the state of the UK market. The number of acquisitions of UK companies by foreign buyers in fact languished at 135, a full 43 per cent below the number reported for 2011, reports the Office for National Statistics.\textsuperscript{14} This trend continued into the first quarter of 2014; the number of inbound acquisitions involving a change of majority ownership fell by 33 per cent on the preceding quarter, but the value leapt from £2.0 billion to £5.4 billion. The increase (£3.4 billion) is precisely equivalent to the consideration paid by Schneider Electric for Invensys in one of the year’s largest transactions. It is important, therefore, to be aware that, notwithstanding the occasional bulge-bracket deal, the UK M&A market remains thin.

There has also been a marked slump in Chinese interest in UK targets following a strong showing in 2011–2012. Of the firm offers announced for Main Market or AIM listed companies in 2013, not a single one involved a Chinese bidder. This is in large part owing to the perceived lack of attractive UK targets in the energy, mining and utilities sectors, to which Chinese acquirers gravitate (of the ten largest Chinese outbound M&A deals in 2013, seven were for targets in the energy sector).\textsuperscript{15} It would appear, however, that Chinese outbound M&A investment is gradually diversifying. Chinese M&A activity in the TMT sector increased by 14 per cent in volume in 2013 relative to 2012, and more than tripled in value to US$3.9 billion, Mergermarket reports. Chinese buyers are also making inroads into the leisure sector, particularly in Europe. It is not unlikely,

\begin{thebibliography}{99}
\bibitem{young} Ernst & Young, \textit{European Attractiveness Survey 2014: Europe’s 2013 FDI map and rankings} (2014).
\bibitem{allen} Allen & Overy LLP, ibid., p. 9.
\bibitem{plc} PLC, ibid., p. 20.
\end{thebibliography}
therefore, that proactive Chinese acquirers, alive to the domestic shift in China from an export-led to a consumer-driven economy, will look to acquire interests in a broader range of sectors in 2014.

One of the most closely watched near-deals of recent months was Pfizer Inc’s bid for AstraZeneca PLC, which valued the UK pharmaceuticals manufacturer at £69.4 billion. The attempt was notable for a number of reasons, but perhaps chiefly for the strong political involvement in the process. Pfizer executives were forced to appear before multiple parliamentary hearings, and pressed to make promises in respect of UK jobs and manufacturing facilities, while politicians began mooting ideas for legislative changes to frustrate the bid (discussed in greater depth below). We have seen a broadly similar story develop in France, as General Electric’s bid for the energy business of Alstom SA was immediately subject to significant political argument and scrutiny. After years of anaemic growth, many European companies may look vulnerable to the advances of acquisitive US rivals, and there may be considerable mileage to be had by politicians protecting (or being seen to be protecting) national champions. It is likely, therefore, that any approaches by overseas bidders on major UK targets will continue to be subject to close political scrutiny (for more detail, see below).

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

i Telecommunications, Media and Technology

The TMT sector was the liveliest sector in EMEA in 2013. There were €97.2 billion worth of deals, representing a 97 per cent upswing from the equivalent figure for 2012, Mergermarket reports. 16 Of the 20 highest value deals in EMEA in 2013, nine were in the TMT sector. The UK has a particularly strong TMT sector, so it is no surprise to see UK companies at the centre of this rush. Of the 15 highest value TMT deals of 2013, five involved UK entities: the sale by Vodafone Group of its 45 per cent stake in Verizon Wireless, the acquisition by Liberty Global of Virgin Media, the acquisitions by Vodafone of Kabel Deutschland and a 23 per cent stake in Vodafone Italia, and BC Partners’ acquisition of Germany’s Springer Science + Business Media. These transactions had a combined value of over €127 billion. In the first half of 2014, Vodafone has again turned to its war chest, vastly increased after the Verizon disposal, to acquire Spain’s Grupo Corporativo ONO for €7.2 billion, and Liberty Global (newly a UK plc) has acquired Dutch cable operator Ziggo for €10 billion.

The reasons underlying what is becoming something of a telecoms land grab in Europe include the continued roll-out of high-speed mobile and wireless networks, and a push for so-called ‘quad-play’ product offerings; that is, bundled products comprising mobile, fixed-line, TV and broadband services. This, together with continued drives for market share and cross-border consolidation, is anticipated to keep the telecommunications market vibrant throughout 2014. In addition, the likes of British Telecom and Liberty Global may be expected to broaden their content portfolios. In

16 Mergermarket, Deal Drivers – EMEA, p. 30.
May 2014, Liberty Global, in concert with Discovery, agreed to acquire All3media for £550 million, and there is speculation that Liberty Global will attempt to wrest the Formula 1 brand from CVC Capital Partners.

Comfortably the largest EMEA deal of 2013, Vodafone’s disposal of a 45 per cent shareholding in Verizon Wireless to Verizon Communications was also the third largest corporate transaction in history and seemed to be the trigger for a rush of subsequent acquisitions. A substantial amount of the sale proceeds was returned to shareholders; US$60.15 billion worth of stock was issued to Vodafone shareholders as part of the consideration and US$23.9 billion returned in cash. The disposal represents a retreat for Vodafone from one of the few growing (and highly profitable) markets for telecommunications companies in the developed world and, perhaps, a narrowing of horizons for the UK company, which will look instead to out-invest its European competitors in the short term. Vodafone has wasted little time in putting the remaining cash from the sale to work.

In June 2013, Vodafone announced its offer for Kabel Deutschland at €87.00 per share (inclusive of a promised €2.50 dividend paid following the acquisition), which represented a 37 per cent premium over the share price immediately preceding the outbreak of takeover rumours. The deal valued Kabel Deutschland at €10.7 billion. The transaction significantly strengthens Vodafone’s German mobile operations and provides it with a launch pad for TV and fixed broadband provision in Germany. It also allows Vodafone to migrate its fixed-line DSL customer base to Kabel Deutschland’s cable network, thereby jettisoning some costly support facilities. There is, finally, substantial upside potential from revenue synergies, including cross-selling. In a further leap toward consolidating its communications strategy in the European market, Vodafone agreed to acquire Grupo Corporativo ONO for €7.2 billion in March 2014. The deal complements Vodafone’s ‘fibre to the home’ venture with Orange, and its ongoing network builds in southern Europe.

In February 2013, Liberty Global announced the acquisition of Virgin Media in a mix of cash and shares. The implied purchase price represented an enterprise value of £14.3 billion. In January 2014, Liberty Global announced the acquisition of Ziggo for €10 billion, which valued the Dutch cable operator at 11 times its projected EBITDA for 2014 (or 9.4 times the same, according to Liberty Global, when projected synergies and the buyer’s prior 28.5 per cent stake are accounted for). The price per share of €34.5 represented a 22 per cent premium to the share price prior to Ziggo’s announcing Liberty Global’s interest. With these additions to its portfolio, Liberty Global seems to be building a pan-European cable and telecoms group and positioning itself squarely in competition with Vodafone in the growing ‘quad-play’ arena. The two groups have been shadow-boxing around each of these transactions: Liberty Global attempted to derail Vodafone’s bid for Kabel Deutschland (meaning Vodafone was forced to hike its offer price), Vodafone was strongly linked with Ziggo, both made overtures to ONO prior to Vodafone’s offer, and both are also rumoured to be mulling bids for other operators like Italy’s Fastweb. Whether this costly dance will continue is uncertain: the Financial Times reports that Vittorio Colao, Vodafone’s chief executive, has mentioned that the
two groups have considered joint venture possibilities. It will also be interesting to observe whether antitrust regulation will begin to bite as the likes of Vodafone and Liberty Global consolidate their pan-European networks. It may be, Mergermarket suggests, that telecoms companies turn increasingly to central and eastern Europe for growth opportunities if EU regulators pour cold water on continued, large tie-ups in the EU core. However, even the Commission appears amenable to telecoms mergers considering the uniquely fractured (and, in some respects, inferior) state of the European telecommunications market. There are between 80 and 100 carriers operating in Europe; in the US, there are four.

ii Pharmaceuticals, Medical and Biotech

The pharmaceuticals, medical and biotech sector enjoyed a solid year in 2013. In Europe generally, 351 deals were completed in 2013, with a total value of €32.5 billion, compared to 312 deals worth €26.0 billion in total in 2012. This represented a 6.8 per cent share of total M&A value in Europe for 2013, placing the sector sixth of 13. The majority of value was, however, realised in the last two quarters of the year, and the start of 2014 has seen a rush of large pharma transactions; there were US$163 billion worth of proposed pharmaceutical deals in the first four months of 2014, reports Dealogic, an increase of 50 per cent on 2013. When Pfizer’s £69.4 billion bid for AstraZeneca is included, this figure grows to record proportions. UK companies have been very much at the centre of this activity.

One of the more interesting recent transactions was GlaxoSmithKline’s three-part inter-conditional agreement with Switzerland’s Novartis. This transaction had three distinct elements: first, the sale by GSK of its marketed Oncology portfolio, related R&D activities and rights to its AKT inhibitor to Novartis (including a grant of commercialisation partner rights for future oncology products) for total consideration of US$16 billion; second, the sale by Novartis of its vaccines business (excluding its flu products) for up to US$7.1 billion to GSK; third, the creation of a consumer health-care business through a joint venture between GSK Consumer Healthcare (with a majority, 63.5 per cent, stake) and Novartis OTC.

The transaction was striking above all for its complexity and the way in which it seems to benefit both parties strategically: each party has divested a part of its business which the other could make better use of and the joint venture business is anticipated to generate US$10 billion in yearly revenues. GSK is left, having shed much of its high-risk oncology portfolio, with a more focused suite of businesses: respiratory conditions, HIV, vaccines, and consumer health care. Novartis has the scale to speed the development of the compounds it has acquired from GSK. Notably, however, in June 2014 GSK announced the acquisition of Adaptimmune, a UK biotech with which it hopes to develop new cancer treatments. The particular type of treatment to be developed is an alternative type of immunotherapy which involves the removal, modification and

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18 Mergermarket, ibid.
19 Mergermarket, ibid., p. 38.
reintroduction of disease-fighting ‘T-cells’, and is of a type that Novartis is also in the process of developing. It seems clear, therefore, that GSK does not wish to discount itself wholly from the oncology market, regardless of the Novartis deal.

It has also been an eventful year for AstraZeneca. In December 2013 it bought out its joint venture partner Bristol-Myers Squibb for US$4.3 billion, thereby securing control of a line of diabetes medicines estimated to be worth around US$1.65 billion in 2013 sales. AstraZeneca appears to be seeking means by which to offset an oncoming decline in revenues as several of its most valuable patents (including the popular statin Crestor) reach the end of their lives. Bristol-Myers, for its part, is looking to slim its operations to several specialist therapy areas, including HIV and oncology. The pressure continued to mount on AstraZeneca into 2014, and there was speculation that the company could make a bid for the biopharmaceutical maker Shire plc (which has also been linked with, among others, Allergan Inc, the US maker of Botox).

The pressure culminated in the approach from Pfizer, which attracted an exceptional amount of public and especially political interest. The potential bid provoked a debate, not merely on the merits or demerits of the proposed tie-up, but more broadly on the appropriate political oversight of UK corporate transactions. Detractors, including many politicians, argued that Pfizer, with a history of making severe efficiency cuts to its acquired businesses, would jettison research jobs and R&D and erode the UK science base. These concerns reached such a pitch that Pfizer was forced to write directly to the Prime Minister, setting out certain commitments it intended to comply with if the acquisition of AstraZeneca was completed. There were also suggestions of direct intervention by the government on the grounds of public interest. Two legal issues emerged out of these developments which are worth considering in some detail: first, the status of commitments made by a bidder company under the Takeover Code; and second, the legal basis for intervention by the Secretary of State in mergers on public interest grounds.

Note 3 to Rule 19.1 of the Takeover Code clearly places an obligation on a bidder company which has made a commitment in any offer documentation to abide by that commitment. There is, however, an ‘escape clause’ if there is a material change of circumstances. The Takeover Code does not provide guidance on what may amount to a ‘material change of circumstances’; it would be for the Takeover Panel to decide whether any particular change in circumstances was sufficiently material to allow the commitment to be avoided. It appears that the government may have been content to rely on the Takeover Code to ensure Pfizer’s commitments were complied with. However, the scope for government to engage in negotiations of the terms of such commitments is not unconstrained. Any commitment seen as arising from a de jure or de facto government requirement could raise EU law considerations of the type outlined below. It would, however, be more difficult to bring an EU law challenge against enforcement of unilateral statements voluntarily offered by the bidder.

The Secretary of State has the power to intervene in mergers on certain public interest grounds by issuing an intervention notice to the Competition and Markets Authority. Where such an intervention can be made, approval of the deal can be made conditional upon commitments from the acquirer. A public interest intervention could, therefore, have enabled the Secretary of State to obtain direct undertakings from Pfizer which would have been binding over the long term. The problem, however, is that the
existing public interest grounds relate to national security, various media issues and financial stability, and would not therefore easily have accommodated the concerns around the proposed Pfizer bid. It was open, however, to the Secretary of State to introduce a new public interest consideration. Such a step would likely have required the approval of Parliament which, if there was sufficient political support in the UK to intervene in the deal, may well have been forthcoming. It would, however, have been considerably more problematic to secure confirmation from the European Commission that such a step was consistent with EU law. The Commission, keen to deter national governments from cluttering the ‘one-stop shop’ nature of EU merger control, is not in the habit of approving Member State intervention on new public interest grounds. The UK government would also have had to convince the Commission that its intervention would not have discriminated in favour of the UK over other EU Member States. This would have complicated proposals, for example, to require Pfizer to base its European headquarters in the UK or to ensure that a specified percentage of its R&D workforce is based in the UK. The provisions of EU law may have meant that any commitments extracted from Pfizer under a public interest intervention were necessarily generic and non-UK-specific; the precise opposite, in other words, of what the politicians were looking for.

It is significant that, in an analogous set of circumstances in France, the French government on 14 May 2014 issued a decree purporting to extend its jurisdiction to intervene in foreign takeovers in strategic sectors. It is believed that this move is linked to the political controversy surrounding the potential acquisition of Alstom’s energy assets by General Electric. The French government may be able to successfully argue that its action relates to public security, and is therefore consistent with EU law, but much depends on the manner in which the French government seeks to implement the decree in practice. European Commissioner Michel Bernier has warned that the French measure will be ‘examined very thoroughly against the backdrop of European legislation’.

The frailty of the European economic recovery means that national governments are acutely sensitive to what they perceive as aggressive overseas acquirers. It is not at all inconceivable that the UK government, and governments across Europe, will attempt to intervene in the future more overtly than we have seen in the past if major UK and European targets are subject to foreign takeover bids.

VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

i Public M&A financing

Of the 33 firm offers announced in 2013 reviewed by PLC’s ‘What’s Market’ where the consideration was at least partially in cash, the bidder’s cash resources alone were the means of financing in 17 of those offers. In five of those bids, cash was provided to the bid vehicle by an inter-company loan from the bid vehicle’s shareholders. Debt facilities were used by bidders in 11 offers. Two of the offers announced in 2013 combined debt and equity financing: The Stanley Gibbons Group plc’s offer for Noble Investments

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20 PLC, ibid., p. 17.
(UK) plc involved a fully underwritten cash placing which raised some £40 million, and Source BioScience plc’s raised £9.5 million in a placing to fund its offer for Vindon Healthcare plc.

PLC also noted that, in a number of offers, the Takeover Panel granted a dispensation from Rule 24.3(f) of the Takeover Code, which provides that bidders must disclose details of how the offer is to be financed. Rule 26.1(b) provides that such a description must be published at the time of the announcement of the firm offer. Descriptions of debt facilities which will finance the offer must also be disclosed, including details of any market flex provisions in those facilities. Concern has been expressed that such a disclosure has the potential to swell the bidder’s cost of financing; if potential syndicatees are privy to the parameters within which a lead arranger is willing to provide finance, they may have the leverage, in negotiating the facility, to push pricing to the higher end of the flex. The Takeover Panel, therefore, waived the requirement of Rule 26.1(b) in respect of a number of offers announced in 2013.

The effect of such a dispensation is that the bidder's lender has a grace period of 28 days in which to syndicate the loan, before the offer document must be published. If the loan has been syndicated by that date, the offer document need not disclose any market flex provisions (as they will, by then, be irrelevant). The requirement remains, however, if the facility has not been syndicated by that date. It is of potential significance that a dispensation was not granted in respect of Schneider’s offer for Invensys, one of year’s largest deals. It is not known whether such a dispensation was sought but, if it was, it may suggest that the Takeover Panel is less inclined to relax the Code in respect of larger borrowers, where debt facilities will typically be more tightly priced.

ii ‘Cov-lite’ loans and the search for yield

The search for yield is continuing to grow the market in ‘covenant-light’ loans, both in the US and, increasingly, in Europe. Dollar-denominated cov-lite loans to US and European companies reached a record US$260 billion in 2013, representing 57 per cent. of the total volume of loans, reports the Financial Times. These loans, which are devoid of standard financial maintenance covenants (such as, for example, leverage and interest ratio), are a hallmark of generous credit markets, but have traditionally been confined to the US. However, there has been a record increase in the amount of cov-lite loans being issued in euros: nearly €8 billion of such loans were issued in 2013 (a higher figure than the €7.73 billion recorded for 2007).

In March 2014, Ceva Santé Animale, the French veterinary drug producer, became the first European borrower to secure a purely euro-denominated cov-lite debt package from a syndicate which included Goldman Sachs and Nomura (previous issues have always incorporated a dollar tranche). What is even more remarkable is that the Ceva debt facility does not have the protection of a ‘double luxco’ structure, meaning that lenders are unable to enforce security in the event of default without proceeding through the French courts. In the wake of Ceva’s success, French foodmaker Diana Ingredients

22 Ibid.
has also proposed, as part of its ongoing auction process, an €800 million all-euro cov-lite facility on the basis that the sale is made to a private equity house.

In other respects, too, lending is becoming increasingly borrower-friendly. One indicative deal of 2013 was the package issued to CVC Capital Partners for its purchase of Ista International. The facility incorporated only two of the four traditional maintenance covenants, the debt to EBITDA ratio was extremely high (7.2 times), and the loan was priced at 400bp over Euribor, comfortably below the suggested range of 450bp–475bp. In spite of all this, the book was heavily oversubscribed. The hunt for yield is also enabling issuers to leverage to a degree not seen since 2007; the Ceva deal will result in Ceva’s total debt being equivalent to 7.5 times EBITDA, and lenders are reportedly offering debt worth up to 6.25 times EBITDA to finance the €1.2 billion acquisition of Mauser, a German packaging group. Other borrower-friendly terms re-emerging in the markets include portability provisions, which allow an issuer’s existing debt to remain in place upon a change of control. The French catering company Elior made a request for such a provision in March 2013, and it would not appear unlikely that similar requests will be made by other issuers as lenders continue to loosen borrower constraints.

### Bridging loans

Another result of the buoyant equity markets is an increasing use of bridging loans in investment grade acquisition finance. The financing of Verizon Communications’ purchase of Vodafone’s 45 per cent. shareholding in Verizon Wireless is telling, EuroWeek suggests, of the appetite of banks and investors for cheap debt. The acquisition was part-funded by a US$61 billion, 364-day bridge loan, reportedly the largest bridge loan in history. The loan included a US$12 billion bridge-to-term loan tranche A, and a US$49 billion bridge-to-bond tranche B. Demand for the bond tranche was so high that the bond was enlarged to US$49 billion from a planned US$20 billion, making it three times the size as the previous largest corporate debt sale in history (Apple’s US$17 billion bond issue of April 2013).

Other recent deals which have made use of bridging facilities include Bayer’s acquisition of US health-care company Merck for US$14.2 billion, which is to be part-funded by a jumbo US$12.2 billion bridge to bond priced at 25bp, and Schneider Electric’s acquisition of Invensys, which was financed with a £1.5 billion bridge priced at 30bp. Lenders are showing little reticence to underwrite bridges on a big ticket basis, such is their confidence in an eventual capital market take-out. Competition between banks is reportedly so strong that bridges are increasingly tightly priced, and the chief draw is rather that the lending banks will have the opportunity to pick up some ancillary business in the eventual refinancing. Typically, however, bridges continue to incorporate ‘ticking fees’ for the period between the loan being made available and being drawn down, and margin step-ups and duration fees to encourage timely refinancing. The Verizon bridge, for example, paid a 10bp ticking fee, 25bp quarterly margin step-ups and quarterly duration fees on amounts outstanding for one year beyond the maturity date.

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23 Ibid.
The willingness of banks to allow for looser borrower constraints, to underwrite jumbo facilities in small syndicates, and to offer flexible and fast bridge financing for high-value acquisitions, presents a financing climate that should be particularly amenable to corporate M&A.

VII EMPLOYMENT LAW

i TUPE: 2014 amendments

The most significant recent employment law development of relevance to M&A transactions is the amendments that have been made to the Transfer of Undertakings (Protection of Employment) Regulations 200625 (TUPE). The amendments were made in January 2014 following a consultation which had the stated aim of improving and simplifying TUPE for all parties involved in business transfers. The extent to which this objective will be achieved remains to be seen.

The amendments were implemented via the Collective Redundancies and Transfer of Undertakings (Protection of Employment) (Amendment) Regulations 201426 (CRTUPE 2014) and the Occupational Pension Schemes (Miscellaneous Amendments) Regulations 201427 (OPSMAR 2014).

The main changes made by CRTUPE 2014 are:

Relaxing the restrictions on dismissals and changes to terms and conditions

Under the amended Regulations 4 and 7 of TUPE, dismissals and changes to terms and conditions will only be restricted where they are ‘by reason of transfer’ itself. The previous restriction ‘for a reason connected with the transfer’ has been repealed. Although this appears to give employers more freedom, the exact scope of the new wording is as yet untested. What is clear is that notwithstanding the change, purchasers may still find it difficult to make changes to harmonise the terms and conditions of staff inherited on a TUPE transfer with their existing workforce. However, one useful change is that employers will more readily be able to make changes to terms and conditions and dismiss employees where the transfer will involve a change in location of the workforce; a situation which would often trigger liability for purchasers under the previous regime.

Pre-transfer redundancy consultation

There is a new regime under Sections 198A and 198B of the Trade Union and Labour Relations (Consolidation) Act 1992 (TULR(C)A 1992), which allows the purchaser to undertake collective redundancy consultation pre-transfer, if it proposes making collective redundancies post-transfer. There was uncertainty about whether this was possible under the previous regime, which often resulted in delays and separate consultation processes under TUPE and TULR(C)A 1992. Under the new regime the purchaser may choose to begin the redundancy consultation process pre-transfer, but only if the seller consents.

25 SI 2006/246.
26 SI 2014/16.
27 SI 2014/540.
The process is then effectively run by the purchaser; there is no duty on the seller to cooperate or provide assistance, unless the parties contractually agree otherwise (which will be advisable in most cases).

**Collective agreements**

Regulation 4A of TUPE now makes it clear that the purchaser is only bound by collective agreements in the terms in force at the time of the transfer, and not by any future changes to those collective agreements, if the purchaser is not a participant in the collective bargaining for those changes. This is designed to implement the recent decision in *Alemo-Herron and ors v. Parkwood Leisure Ltd* \(^28\) (see Section V of Chapter 1 for further consideration of this case). In addition, Regulation 4(5B) now allows variations to contractual terms incorporated from collective agreements, provided that they take place more than one year after the transfer, and that the employee's contractual rights and obligations remain no less favourable overall.

**Service provision changes (SPCs)**

The consultation proposal to repeal the SPC provisions of TUPE has not been implemented. Instead, there is a new express requirement that following the SPC, the activities carried out by the new service provider must remain fundamentally the same. This broadly reflects existing case law, so will have little practical impact.

**Employee liability information (ELI)**

Again, the consultation proposal to repeal the requirement for the seller to provide ELI has not been implemented. Instead, the deadline for the provision of ELI has been increased from at least 14 days to at least 28 days before the transfer. This change will have little practical impact where ELI is dealt with as part of the usual due diligence process, although it may place a greater emphasis on the seller’s duty to keep the ELI up to date.

**Micro-businesses**

Regulation 13A of TUPE eases the burden on micro-businesses (those with fewer than 10 employees) by exempting them from the requirement to elect employee representatives for TUPE consultation. This means that unless appropriate representatives are already in place, the micro-business can inform and consult its employees directly. This change will not only assist small businesses; it will also apply to subsidiaries of larger companies, where the subsidiaries only employ fewer than 10 employees.

On the pensions side, OPSMAR 2014 amends the pension protection requirements which apply to a purchaser following a TUPE transfer, to take account of the auto-enrolment regime. The changes apply where the purchaser intends to use either a defined contribution scheme or a stakeholder scheme; the pension protection requirements in respect of defined benefit schemes remain unchanged.

\(^{28}\) [2013] EUECJ C-426/11.
The changes allow the purchaser the option of matching the transferor’s level of employee contributions immediately before the transfer, or (as currently) matching the employee’s chosen contribution rate up to 6 per cent. The changes are intended to prevent a situation where a purchaser must pay a higher level of contributions than either the seller or that required by the auto-enrolment regime.

Overall, the TUPE amendments are favourable to employers. Although it is too early to assess the full impact in practice, it is hoped that they will ease the regulatory burden on parties to a business transfer.

ii Collective redundancies

The obligation to consult employees on collective redundancies under Section 188 TULR(C)A 1992 is another area which often comes into play on M&A transactions. The obligation is triggered ‘where an employer is proposing to dismiss as redundant 20 or more employees at one establishment within a period of 90 days or less’ (Section 188(1) TULR(C)A 1992). Until recently, this required an analysis of how many redundancies the employer was proposing at each establishment. From the employer’s perspective, the aim was always to try to define the establishment as narrowly as possible; the smaller the establishment, the less likely that the collective consultation obligations would be triggered.

However, this approach has now been fundamentally altered by the decision in *USDAW & anor v. Ethel Austin Ltd & ors*, 29 the case which arose out of the administration of Woolworths plc. The administrator had treated each Woolworths store as a separate establishment, and many of the stores had fewer than 20 employees. This meant that the obligation to consult collectively about the closure of the stores (and the consequent redundancies) had not been triggered in respect of the smaller stores with fewer than 20 employees. The employees of those stores were therefore not entitled to receive a protective award, even though the Tribunal found that the administrator had failed to comply with its collective consultation obligations. The result was that 3,233 of the more than 27,000 employees of Woolworths who were made redundant did not receive a protective award.

The EAT overturned the Tribunal’s decision. It decided that the ‘at one establishment’ limitation was not compliant with the underlying EU Collective Redundancies Directive. 30 It therefore, controversially, decided that Section 188(1) TULR(C)A 1992 should be read as if the words ‘at one establishment’ were not included. The case has since been referred to the European Court of Justice (ECJ) to determine what the correct position is, but pending the ECJ’s judgment, the EAT’s decision stands.

The implication for employers is that collective redundancy consultation obligations will be triggered more readily than before. These obligations will arise whenever an employer proposes 20 or more redundancies within a period of 90 days or less, across its whole business. This means that every time redundancies are proposed, the employer needs to consider whether redundancies are also proposed in other parts of

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29 [2014] EWCA Civ 142.
30 98/59/EC.
its business. This will require employers to have more central oversight of redundancies throughout the business.

Redundancies are often a feature of M&A transactions, and the collective consultation requirements, if triggered, can impact significantly on the timetable for the transaction, as well as creating additional administrative burdens for the employer. The parties should therefore consider at an early stage whether the collective consultation regime is likely to apply, and factor this in to the transaction structure.

iii Historic liabilities for holiday pay

Another hot topic currently is the calculation of holiday pay, and the potential for historical mistakes in the calculation to give rise to significant liabilities.

The calculation of holiday pay is governed by the concept of ‘a week’s pay’ in Sections 221–224 of the Employment Rights Act 1996. The mechanism is complex, and depends on whether the employee has normal working hours and whether their remuneration varies depending on the type or amount of work done. The effect is that in some cases it is not simply base salary which is taken into account in the calculation. Additional payments such as overtime, bonuses, commission, and allowances may also need to be added in (increasing the value of holiday pay). This issue was highlighted by the recent British Airways plc v. Williams litigation, in which the ECJ 31 and then the Supreme Court 32 confirmed that employees were entitled to receive holiday pay which included allowances and supplementary payments which were ‘intrinsically linked’ to the performance of their contractual duties. In the months that followed, the retailer John Lewis paid out £40 million to employees after admitting that it had miscalculated holiday pay across the business by failing to take into account overtime payments in the calculation of holiday pay.

Most recently, in Lock v. British Gas Trading Limited 33 the ECJ has confirmed that the EU Working Time Directive 34 (WTD) requires that workers must not suffer a reduction in their remuneration as a result of not earning commission during periods of annual leave. The case concerned an employee of British Gas who suffered a drop in his remuneration reflecting the commission which he did not earn during his Christmas holiday. The ECJ held that the WTD requires that workers must receive their ‘normal remuneration’ in respect of periods of annual leave, on the basis that any reduction may deter them from taking that leave. ‘Normal remuneration’ for these purposes should include any payments which are directly linked to the employee’s work within the company (whether contractual or not). As Mr Lock’s commission satisfied this test, the ECJ concluded that he should therefore be paid a sum representing the average amount of commission that he would have earned had he not been on holiday.

This has led to a concern among some businesses that they may face similar exposure for unpaid holiday pay. The risk is that from a legal perspective such claims can

33 [2014] EUECJ C-539/12.
34 2003/88/EC.
potentially be made over a period stretching back to the introduction of the Working Time Regulations\textsuperscript{35} in 1998. Any such claims would need to be made within three months of the last incorrect payment of holiday pay.

In an M&A context, this issue may be material in industries with atypical remuneration structures and a high proportion of overtime and bonuses, particularly on transactions involving significant numbers of employees. Purchasers in these circumstances should consider seeking an indemnity to cover any potential historic liability for holiday pay.

\textbf{iv New fair deal policy implemented}

From its introduction in 1999 until early October 2013, the fair deal policy required the provision of broadly comparable occupational pension benefits where staff were compulsorily transferred from the public sector to a new non-public sector employer. Staff were offered the choice of becoming a deferred member of the scheme they were leaving, or transferring their accrued benefits by way of bulk transfer to a new scheme provided or set up by the non-public sector employer.

However, on 4 July 2012 the government had announced that the fair deal policy was to be reformed. Following two consultation exercises, closing in February 2013\textsuperscript{36} and June 2011\textsuperscript{37} respectively, HM Treasury published its new fair deal policy on 8 October 2013.

Under the new policy, staff compulsorily transferred (i.e., by operation of TUPE) from the public sector to an independent contractor will be offered continued access to a public service pension scheme rather than being offered a broadly comparable private pension scheme. Staff will continue to be members of the scheme on the same terms as other members of the scheme, and will be provided with access to the same scheme on any subsequent compulsory transfer. The contract for the business transfer will specifically require the independent contractor to provide transferred staff with continued access to the relevant public sector pension scheme while they remain employed on the public sector contract. From the transferring employer’s perspective, the transaction documentation will be instrumental in limiting the cost of accruals and setting out any exit charge where the public service contracts terminate and the transferring employer leaves the scheme.

A large number of people covered by the new fair deal policy have final salary pension rights. The government’s decision to provide transitional protection to those closest to retirement, and to maintain the final salary link for service in the existing public service pension schemes, means that pay in the final years of an employee’s career will have a direct impact on the cost of providing that employee’s pension. However, under the new Local Government Pension Scheme, LGPS 2014, which went live on

\textsuperscript{35} SI 1998/1833.


\textsuperscript{37} ‘HM Treasury Consultation on the Fair Deal Policy: treatment of pensions on compulsory transfer of staff from the public sector’ March 2011.
1 April 2014, final salary is replaced with career average revalued earnings benefits, with an accrual rate of 1/49th. All pension rights accrued in relation to service to 1 April 2014 are protected and retain a final salary basis. Therefore, the number of public sector employees with final salary pension rights will decrease during the lifetime of the new fair deal policy.

The new fair deal policy came into effect immediately upon its publication and must be reflected in procurement practices as soon as is practicable without disruption to projects that are already at an advanced stage. However, the earlier guidance remains in force where there are 'exceptional' circumstances, which means that staff who were compulsorily transferred should not be given continued access to the public sector pension scheme. For example, if a contract involving compulsory transfer of employees under the old rules is re-tendered, the incumbent need not transfer the employees in question from a broadly comparable scheme to an appropriate public scheme if it would face significant costs in doing so.

v Bridge Trustees v. Houldsworth: new regulations made
The Supreme Court judgment in Bridge Trustees v. Houldsworth decided that certain benefits could be considered money purchase even though it was possible to have a shortfall in their funding. The Department of Work and Pensions responded to the decision by announcing, on 27 July 2011, that they would provide a legislative override. Accordingly, Section 29 of the Pensions Act 2011 – which is expected to come into force in July 2014 – limits ‘money purchase benefits’ to those that cannot have a funding shortfall. When in force, it will take effect back to 1 January 1997.

Section 29 has raised questions concerning retrospective imposition of section 75 debts. Past transactions where schemes had been treated as ‘money purchase’ could trigger Section 75 debts where the schemes would not now fall under the new Section 29 definition. The Pensions Act 2011 (Transnational, Consequential and Supplementary Provisions) Regulations 2014 (the Regulations), which will come into force in July 2014, will help to alleviate this uncertainty. The Regulations ensure that Section 29 will not have retrospective effect for non-compliant schemes that treated ‘non-money purchase benefits’ (i.e., those that do not fall under the new Section 29 definition) as money purchase benefits. Regulation 24 provides two limited exceptions to this rule which, broadly, apply where the employer (or all the employers in the case of a multi-employer scheme) becomes insolvent or is wound up. In the case of these limited exceptions, Section 75 of the Pensions Act 1995 would apply.

vi Extent of pensions exception from TUPE: Procter & Gamble v. Svendka Cellulosa Aktiebolaget SCA
On 14 May 2012, the High Court (Hildyard J) held that entitlement to enhanced early retirement benefits under a DB pension scheme were not within the pensions exception under Regulation 10 of TUPE and so transferred on the transfer of a business in which

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38 [2011] UKSC 42.
members of the scheme were employed. However, only enhanced benefits payable up to the scheme’s normal retirement age transferred; benefits payable after that age were ‘old age benefits’ within the pensions exception.

The High Court’s decision gave rise to a number of practical difficulties not addressed by the Court. For example, it is not clear how entitlement to enhanced early retirement may be valued and so factored into the consideration paid for a business where such entitlements will transfer under TUPE. In addition, the judge did not consider future service benefits applicable to employment after the transfer. The purchaser could, therefore, be obliged to provide enhanced benefits with reference to future salary increases for the period until normal retirement date. Clarification from the Court of Appeal would have been helpful to address these practical issues.

In January 2014, BIS issued guidance on the application of TUPE to pensions.40 The guidance does not specifically reference Procter & Gamble, although it does state that the pensions exception from TUPE is ‘construed narrowly’. According to the guidance, this means that ‘rights relating to redundancy and early retirement benefits […] are likely to transfer’.41 It had been hoped that guidance from BIS on the application of TUPE to pensions would be issued following the High Court decision. The January 2014 guidance has not provided much in the way of further clarification in the wake of the decision and the subsequent settlement of the case.

VIII TAX LAW

i GAAR and other anti-avoidance measures

Introduced in 2013, the general anti-abuse rule (GAAR) contains two tests: are there arrangements that have as a main purpose securing a tax advantage? And if so, are they arrangements the entering into or carrying out of which cannot reasonably be regarded as a reasonable course of action? This is to be assessed ‘having regard to all the circumstances’, including: (1) consistency with policy objectives; (2) whether there are any contrived or abnormal steps; and (3) whether the arrangements exploit any shortcomings in the relevant provisions. If the GAAR applies, HMRC can counteract the tax advantage by making ‘just and reasonable’ adjustments.

As predicted, the GAAR has had little effect so far on corporate taxpayers as they had already begun to adopt a more conservative approach to tax planning. If HMRC sticks to the government’s commitment to catch only ‘egregious’ or ‘artificial and abusive’ schemes with the GAAR, most corporate groups will have little to fear.

Meanwhile the government continues to chip away at schemes that are not aggressive but are nevertheless disliked by HMRC, by using specific anti-avoidance rules for particular schemes or more general but (in name at least) targeted anti-avoidance rules (TAARs). Regrettably, there is an increasing trend for anti-avoidance provisions to be drafted very broadly and for the ‘innocent’ transactions to be taken out of the legislation by guidance. This is evident, for example, in two sets of rules contained in Finance Bill

2014, aimed at partnerships formed by a mixture of individuals and companies and at the tax-motivated transfer of profits within groups of companies.

ii  Tax and procurement

Potential suppliers to the government are now required to confirm their tax compliance as part of the procurement process for all central government contracts with a value of £5 million or more. If a supplier has had an ‘occasion of non-compliance’ since 1 April 2013, the contracting department has discretion to exclude that supplier from the procurement process.

The new EU Directive 2014/24/EU on public procurement (the New Directive), replacing Directive 2004/18/EC, is due to be transposed into national law by early 2016 and this may occur sooner in the UK. The text raises questions over the legality of some aspects of the UK legislation.

Under the New Directive, a bidder will be subject to mandatory exclusion from the procurement process where it has been established by a final judicial or administrative decision that it has breached its tax payment obligations, or discretionary exclusion where there is an existing demonstrable breach of the bidder’s tax payment obligations.

The inability of the contracting authority to exercise discretion where there has been a final decision or judgment appears to be at odds with the UK approach, as does the current £5 million threshold.

On the other hand, the New Directive provides that where a bidder has paid or agreed to pay the tax due, the mandatory and discretionary grounds for exclusion will not apply. There is no equivalent rule in the UK legislation.

iii  Losses on a change in ownership

Like many other jurisdictions, the UK has rules that can deprive a company of carry-forward losses if there is a change in its ownership. The policy objective is to combat loss-buying but the rules can easily apply where there is no tax motivation or for the change in ownership. Relief is restricted for trading losses in two situations: when in any period of three years there is both a change in company ownership and ‘a major change in the nature or conduct of a trade carried on by the company’; and where a change in ownership occurs at any time after the scale of the company’s trading activities has become small or negligible and before any significant revival of the trade.

Similar rules apply for various other losses including, in particular, management expenses and loan relationship debits, where there is a change in the ownership of a company with an investment business. These rules go even further, as they apply not only where there is a major change in the investment business (or it becomes small or

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42 See Article 57, paragraph 2.
43 A change in company ownership occurs when someone acquires more than half of a company’s ordinary share capital. The rules can also apply on a change of indirect ownership. However, a change in the direct ownership of a company is disregarded if the company concerned is a 75 per cent subsidiary of the same ultimate parent company immediately before and after a change of ownership.
negligible) but also where there is ‘a significant increase in the amount of the company’s capital’ following a change in ownership.

Finance Bill 2014 contains legislation which, once enacted, will ease the rules for changes in ownership on or after 1 April 2014; HMRC’s stated intention is to bring the rules more into line with modern commercial practice.

The first relaxation of the rules will mean that the insertion of a new group holding company no longer triggers a change of ownership, so long as the shareholdings in the new holding company mirror those in its predecessor. However, there are likely to be practical difficulties satisfying the exacting requirements for mirror holdings if they remain as drafted. Further, the acquirer must be a ‘new company’: it must not have issued any shares other than subscriber shares or begun to carry on or make preparations for carrying on any trade or business prior to the acquisition. What if the new company puts the subscribers’ cash on deposit, enters into any contractual obligations, engages professional advisers (or enters into other contractual obligations) or registers for VAT prior to the acquisition?

The second relaxation is probably more important (though it will not help trading companies). Under the new rules, an increase in capital will be significant if (in the three years following change in ownership) the capital increases by £1 million or more and is 125 per cent or more of the amount before the change in ownership; in other words, the increase will have to be significant in comparative terms. However, the detail of the rules remains fiddly and ensuring that they do not apply will in many cases continue to be an onerous task.

So the changes are welcome but, in the absence of a motive defence, they will remain a problem for some entirely commercial transactions.

iv Exit taxes

The UK imposes a corporate exit charge on assets within the chargeable gains regime and also on loan relationships (corporate debt), derivative contracts and intangible fixed assets. Following the National Grid Indus case and a request by the Commission for the UK to change its rules, a UK taxpayer can now opt to defer this exit charge by entering into an exit charge payment plan. However, the deferral is time-limited (rather than lasting until realisation of the asset) and interest is charged from the date the normal exit charge would have been payable until the date the deferred tax is paid.

In DMC GmbH v. Germany, the Court of Justice of the EU (CJEU) considered the German corporate exit tax and followed and extended earlier case law on exit taxes (including National Grid Indus), without the need for an Advocate General’s opinion. The CJEU concluded that a Member State may impose a tax on unrealised capital gains generated in its territory so long as (1) the charge does not go beyond what is necessary to attain the objective of the preservation of the balanced allocation of the power to impose taxes between Member States, and (2) where the taxable person elects for deferred payment, the requirement to provide a bank guarantee is imposed on the basis of actual

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44 (C-371/10).
45 (C-164/12).
risk of non-recovery of the tax. The deferral in this case did not last until realisation of the gain (which is what National Grid Indus suggested would be proportionate), but took the form of a spreading of the tax charge calculated on exit.

The case is important and favourable to the UK because the UK’s revised rules work on the basis of such a deferral (payment in instalments is one of the options). There was, however, no requirement to pay interest under the German exit charge, so it still remains to be seen whether this aspect of the UK’s rules (which effectively puts the taxpayer in the same economic position as an immediate charge on exit) would pass the proportionality test.

IX COMPETITION LAW

i Revision of the UK merger regime

On 1 April 2014, the new Competition and Markets Authority (CMA) took over the competition functions of the Office of Fair Trading (OFT) and the Competition Commission (CC), which were abolished on the same day. This change was enacted by the Enterprise and Regulatory Reform Act 2013 along with a series of additional reforms to the framework for UK competition law enforcement. One of the principal objectives of the reforms has been to strengthen the UK merger control regime by extending the regulator’s formal information gathering powers and to increase its ability to prevent parties from taking pre-emptive steps that may prejudice the outcome of an investigation. The reforms are also intended to streamline the merger control process through the use of new statutory time limits and by capturing the efficiencies of having a unitary authority.

Under the new CMA regime, separation is retained between a Phase 1 review (previously undertaken by the OFT) and a Phase 2 review (previously undertaken by the CC). Phase 1 decision-making is now undertaken by the Senior Director of Mergers (or another senior CMA official). Phase 2 decision-making is undertaken by an independent panel of experts. In much the same way as CC panels were formed under the old system, these experts are drawn from a pool of senior experts in a variety of fields.

Notification continues to be ‘voluntary’ in the sense that there is no obligation to apply for CMA clearance before completing a transaction. The CMA may, however, become aware of the transaction through its market intelligence functions (including through the receipt of complaints) and impose interim orders preventing further integration of the two enterprises pending its review. There is a risk that it may then refer the merger for a Phase 2 investigation, which could ultimately result in an order for divestment.

The CMA has a statutory time limit of 40 working days at Phase 1 to reach a decision. It may, however, extend this period in certain exceptional circumstances such as if it is waiting for information from the merging parties. Information can now obtained at Phase 1 through formal information gathering powers with penalties for non-compliance.

While undertakings in lieu of reference to the CC had to be given in anticipation of an adverse decision, under the new regime, the merging parties have five working days from the substantial lessening of competition decision (the ‘SLC decision’) to offer undertakings to the CMA (although may still offer them in advance should they wish to
do so). Where the parties offer undertakings, the CMA has until the tenth working day after the parties received the SLC decision to decide whether the offer might be acceptable as a suitable remedy to the substantial lessening of competition. If the CMA decides the offer might be acceptable, a period of negotiation and third-party consultation follows. The CMA is required to decide whether to accept the offered undertakings, or a modified form of them, within 50 working days of providing the parties with the SLC decision, subject to an extension of up to 40 working days if there are special reasons for doing so.

There is no change to the basic statutory timetable for Phase 2 review: the CMA must issue its decision within a statutory maximum of 24 weeks, extendible in special cases to a period of up to eight weeks. However, the CMA now has a statutory period of 12 weeks (which may be extended by up to six weeks) following the Phase 2 review within which to make a decision on any remedies offered by the parties (no fixed period was previously imposed upon the Competition Commission to consider any remedies offered by the parties following its final report).

The CMA also has stronger powers to suspend or reverse all integration steps in either proposed or completed mergers; and severe financial penalties may be imposed for breaches of any interim orders or undertakings (capped at 5 per cent of the aggregate group worldwide turnover).

ii Treatment of mergers by the OFT and Competition Commission

The number of merger decisions made by the OFT in its final year of operation (65) was significantly lower than in the 2012–2013 financial year (100). This represents a further decrease from the peak of 2010 merger decisions made in the 2005–2006 financial year. Of these 65 cases, eight were referred to the CC and only one involved the acceptance of undertakings in lieu of a reference decision. However, the proportion of cases reviewed by the OFT that were referred to the CC decreased only slightly from 14 per cent to around 12 per cent.

Of the eight references made to the CC during the 2013–2014 financial year, three transactions were cleared unconditionally, two were cleared subject to divestment or the rarer behavioural remedies and three investigations were transferred to the CMA on 1 April 2014. In its final year of operation, the CC published ten final reports on merger inquiries: six were unconditional clearances, two were permitted to proceed only on condition of partial divestments, one on condition of a behavioural price control remedy and the first proposed merger between NHS Foundation Trusts was prohibited.

iii Statements and guidelines relevant to mergers published in 2013/14

Prior to becoming fully operational on 1 April 2014, the CMA had consulted on various new guidance documents. In January 2014, it published a new set of jurisdictional and procedural merger guidelines, at the same time adopting various existing OFT and CC guidance, notably the OFT and CC joint merger assessment guidelines and the CC guidance on merger remedies. This is reflective of the fact that the changes to the UK merger regime are largely procedural rather than substantive.
Guidance on merger fees

The CMA has also issued revised guidance on how to pay fees due on mergers qualifying for investigation. Fees are now payable on the announcement of the CMA’s decision (or the Secretary of State’s in public interest cases) whether or not to refer the merger for a Phase 2 investigation. The CMA’s practice is to send an invoice to the merging parties after a decision has been announced, and payment must be made within 30 days of the date of the invoice.

Fees vary according to the value of UK turnover of the target:

\[ \begin{align*}
   a & : £40,000 for turnover of £20 million or less; \\
   b & : £80,000 for turnover above £20 million up to £70 million; \\
   c & : £120,000 for turnover above £70 million up to £120 million; \text{ and} \\
   d & : £160,000 for turnover exceeding £120 million.
\end{align*} \]

The fees must be paid to the CMA in sterling, net of any transactional costs, and in strict accordance with the payment methods prescribed in the guidance.

OUTLOOK

The start of 2014 has suggested that a much anticipated resurgence in high-value global M&A is beginning. However, and notwithstanding some headline-grabbing deals, the UK domestic M&A market remains slow. This is in part due to the positive fact that many owners of private companies are electing to list their companies, rather than marketing them to a trade buyer. It is also due, however, to continued corporate reticence and perceived valuation disconnects. What is less likely to be inhibitive is the availability of financing, at least for investment grade corporates. It is hoped that, as UK economic growth gathers pace and corporate confidence grows, the domestic market will pick up.

A number of issues continue to threaten to put the brakes on a revival in M&A. Dealmaking between corporates with Chinese interests may be affected by the aggressiveness with which MOFCOM implements Chinese merger control regulation. A mandatory filing regime for merger control has recently been introduced in Brazil, and a supraregional competition and consumer regime established in the Common Market for Eastern and South Africa. In the UK, the new Competition and Markets Authority has been provided with substantially increased powers. If the M&A market is to make a resurgence, it will be one that is closely supervised by the regulators.

Broader concerns also give cause for caution. There is considerable uncertainty as to how markets will process the tapering of quantitative easing by the US Federal Reserve. In addition, there are concerns around how the funding gap left by huge bank deleveraging will be filled, and centrifugal pressures continue to trouble European legislators. Finally, there are concerns as to the depth of the global economic recovery as growth in the BRIC economies slows. The M&A market, like a weathervane, is sensitive to all these developments.
Appendix 1

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