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2017 Summer review M&A legal and market developments

In this issue...

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We set out below a number of interesting English court decisions and market developments which have taken place and their impact on M&A transactions. This review looks at these developments and gives practical guidance on their implications. Summaries feature below, and you can click where indicated to access more detailed analysis.

Contractual provisions

A number of cases have looked at common contractual provisions on M&A deals.

Interpretation of indemnity for consequences of regulatory claims

The Supreme Court recently upheld a Court of Appeal decision on the scope of a regulatory indemnity from a seller (S) under a share sale and purchase agreement (SPA) for the sale of an insurance broker (T). It took the opportunity to give important further guidance on construction of contracts.

The Court of Appeal had previously decided that the indemnity in the SPA did not cover a claim from the buyer (B) in relation to mis-selling of insurance policies, because the indemnity only caught losses from a customer's making a claim or registering a complaint with the then Financial Services Authority (FSA). By contrast the losses here had arisen from T's self-referring potential mis-selling to the FSA. In its judgment the Court of Appeal had said it did not matter that its interpretation made the indemnity uncommercial for B. Importantly, even though the parties had used language which was capable of more than one meaning, the Court of Appeal had said care must be used in adopting business common sense when interpreting a contract, because the court would not know about the parties' negotiations and terms they had to concede to reach a deal. In upholding the Court of Appeal decision, the Supreme Court gave guidance to reconcile past Supreme Court decisions in this area. It said that the court has to ascertain the objective meaning of the language used. In doing so, the contract must be considered as a whole and the context should

Key lessons

- **Flexible approach**: This guidance allows the courts flexibility in their approach to contractual construction.
- **Merits of unambiguous wording**: The judgment is a reminder of the need for unambiguous drafting, and suggests that the contract should always be considered as a whole and the context taken into account. It is important to consider and address the interaction between alternative contractual protections in the SPA.
- **Drafting tips**: As a drafting matter, B's position might have been better if the different limbs of the indemnity had been separate sub-paragraphs, some of which expressly required a customer claim or complaint to a regulator and some not.

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always be taken into account. However, once the court has established that there are rival interpretations it does not matter if the detailed analysis starts with the wording used or the context, as long as the court balances both approaches. Which should be given more weight will depend on the facts. For example, the natural meaning might be given more weight in a sophisticated contract negotiated and prepared with the assistance of skilled professionals. (*Wood v Capita Insurance Services Ltd.* [2017] UKSC 24)

Unenforceable penalty applying Supreme Court test in *Cavendish Square v Makdessi*

A recent High Court decision in a real estate context has found an unenforceable penalty when applying the test for what amounts to a penalty formulated by the Supreme Court in the landmark decision in *Cavendish Square v Makdessi*.[1]

Under a side letter to a lease a landlord (L) agreed to accept a reduced rent from the tenant (T) for the first five years and a capped rent for the following five years. The side letter allowed L to terminate that arrangement if T breached either the side letter or the lease. During the second five-year period, and following changes of landlord, T missed a rent payment due to uncertainty over who should be paid. L terminated the side letter. The High Court decided that the termination provisions were an unenforceable penalty. It said that T's primary obligation was to pay the lower rent specified in the side letter and otherwise comply with all the other obligations of the lease. T's obligation to pay the higher rent was a secondary obligation triggered on breach of the primary obligation. It was not proportionate to protecting L's legitimate interests, because that would suggest L had an interest in T's non-performing rather than performing its obligations. It was exorbitant or unconscionable, taking into account that the termination provision applied on breach of any of T's obligations as tenant, irrespective of the particular impact of the breach, and was expressed to be retrospective too. (*Vivienne Westwood Ltd. v Conduit Street Development Ltd.* [2017] EWHC 350 (Ch))

Key lessons

- **First unenforceable penalty applying the new test**: This appears to be the first English court decision finding an unenforceable penalty since the Supreme Court formulated the new test for what amounts to a penalty under English law in *Cavendish Square v Makdessi*.
- **Failure to distinguish between severity of breach**: In line with historic case law, it was significant to the outcome that the termination provisions imposed a single and significant detriment on the party in breach irrespective of the seriousness of the breach.

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Liability for information on website and applicability of disclaimers

A Court of Appeal decision has supported the workability of disclaimers in information memoranda and raised some important issues.

Bank R had issued loan notes to M, which M on-sold to D. T bought the loan notes from D in the secondary market. R went into bankruptcy. T alleged R had misrepresented its financial position in an investor presentation document which R had produced for a past roadshow (not attended by T) and then published on its website. R had directed potential investors in the secondary market to the presentation there. The Court of Appeal decided that, because R had directed potential investors to the presentation on its website, the disclaimer in the presentation that it was only for roadshow investors was ineffective. However, on the facts the other disclaimers in the presentation worked to exclude liability for damages (for example, as to no representation and

Key lessons

- **Efficacy of disclaimers in information memoranda**: The judgment supports the workability of disclaimers of liability in information memoranda and other non-contractual notices.
- **Duty-negating clauses**: The judgment demonstrates the merits of using duty-negating disclaimers to limit the nature and scope of statements in a document.
- **Publication of documents on websites**: The judgment indicates that in principle investors may be able to rely on the contents of a document on a website when they have been directed to it, irrespective of a disclaimer that it was prepared for someone else.

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1 [2015] UKSC 67.

no reliance). It did not matter that the disclaimers were contained in a non-contractual notice rather than a contract, because the disclaimers and the representations were in the same document. They were duty-negating clauses which made it clear that they could not be relied on as a basis for a decision of any kind. Likewise, there was no reason why certain liability-negating clauses in the presentation (such as that no liability was accepted) were not effective. In any event, the judge at first instance should not have awarded damages under s.2(1) of the UK Misrepresentation Act 1967, because this section only applies where a person has entered into a contract after a misrepresentation by the other contracting party. By contrast, the relevant contract here was with D but the alleged misrepresentation was by R. (*Taberna Europe CDO II PLC v Selskabet* [2016] EWCA Civ 1262)

Obligation to use all reasonable endeavours to obtain senior debt facility enforceable but no good faith term implied

The High Court decided that an obligation to use all reasonable endeavours to obtain a senior debt facility was enforceable, although it had not been breached on the facts, but the court would not imply a duty of good faith to obtain senior debt finance.

A agreed to sell shares in a dormant copper mine to T. T had to pay deferred consideration if it took out a senior debt facility to fund restarting the mine. T and its subsidiaries agreed to use all reasonable endeavours to obtain the facility by an agreed date. Despite several attempts they were unable to do so. T raised equity funds instead which it lent to a subsidiary, and the mine was restarted without triggering the deferred consideration. The High Court decided that the obligation to use all reasonable endeavours here was enforceable, although it had not been breached on the facts. Previous case law had been cautious about enforceability of endeavours obligations to enter into an agreement, particularly where the counterparty would be a third party rather than the recipient of the endeavours obligation. The difficulty has been lack of objective criteria for evaluating whether it was reasonable or unreasonable to have failed to agree the contract. The High Court disagreed and said that it should almost always be possible to give sensible content to such an obligation. In any event, any complaint about lack of objective criteria did not affect enforceability, but merely assessment of whether the endeavours used were reasonable. The court also decided that there was no implied term of good faith to take out a senior debt facility and, even if there had been, it would not have been breached where there had been no breach of the underlying endeavours obligation. Application has been made for permission to appeal the judgment. (*Astor Management AG v Atalaya Mining plc* [2017] EWHC 425 (Comm))

Key lessons

- **Identify key terms up front**: Despite this judgment, where an agreement contains obligations to enter into a further document, it remains advisable to specify its key terms up front and to set objective criteria by which the court can evaluate whether it was reasonable or unreasonable for the contract not to have been agreed (such as steps the obligor should take or need not take and any time limit on the obligation).
- **Agreements to agree remain unenforceable**: It remains the case that the court will not enforce an agreement to agree and will not re-write a contract or substitute terms that the parties have failed to include themselves.

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Consequential loss: wide interpretation on construction of agreement

The High Court recently gave the expression "consequential loss" a wider interpretation than its traditional meaning of indirect losses arising from special circumstances which the party in breach knew about at the date of the contract.

A buyer (B) entered into a contract with a shipbuilder (S) to acquire a ship. Under the contract, S guaranteed the ship for 12 months from all defects from materials and workmanship, undertaking to make all necessary repairs or replacements. However, defects arising from other causes were not guaranteed. The contract also had an exclusion clause stating that, save as expressly provided, S would not have any liability whatsoever in respect of the ship and, in any event, would have no liability for consequential losses. There was a dispute over liability for financial losses arising from engine failure. The High Court decided that the word "consequential" was used in the agreement in a cause-and-effect sense of meaning losses as a result or consequence of the physical damage caused by guaranteed defects, in other words additional financial loss other than the cost of replacement or repair. The effect was that S was not liable. The clause set a complete code of conduct. S only agreed to repair or replace defects falling within the express guarantee, on the basis that all other financial consequences were excluded. (*Star Polaris LLC v HHIC – PHIL INC* [2016] EWHC 2941 (Comm))

Key lessons

- **Clear and unambiguous drafting desirable**: The case shows the merits of clear and unambiguous wording when drafting exclusion clauses and limitations of liability.
- **Natural meaning when interpreting exclusion clauses**: The court will give the words their natural meaning when interpreting exclusion clauses in commercial contracts between sophisticated parties. They will only be interpreted narrowly against the party relying on them in cases of ambiguity.
- **Complete code of damages:** Having an express and complete code of liability assumed, on the basis that everything else is excluded, may have merit for a party assuming contractual obligations.
- **Use of terms of art:** Even where there is previous case law on the meaning of a term, the court may interpret the same formulation differently on different facts.

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Alleged oral contract

The Court of Appeal has confirmed that communications after a contract has allegedly been entered into could be taken into account in determining whether a contract was made. It decided that an oral agreement had not been formed on the basis of an offer letter headed "Without Prejudice–Subject to Contract" and a subsequent phone call.

During the phone call a representative of A said that they accepted the offer from G subject to the two conditions that G resend the offer letter in "open and binding form" and that it also provide satisfactory evidence of its ability to fund the transaction. G's subsequent offer letter provided certain further different terms and asked for confirmation of acceptance. It also said it would expire unless accepted within two days. A responded that it did not accept the offer. The Court of Appeal decided that no oral contract had been formed on the basis of the offer letter marked "without prejudice – subject to contract" and the subsequent phone call. It said that it is well established that, when deciding whether a contract has been formed in negotiations, the court will look at the whole course of those negotiations. However, clear evidence was required to waive a "subject to contract" requirement, and the condition on resending an offer in open and binding form was not consistent with an offer that had already been accepted. Further, the subsequent funding letter did not meet the separate condition of providing satisfactory evidence that G could fund the transaction, as it was subject to a number of matters including satisfactory completion of due diligence and, in any event, expressly stated that it was not intended to create a contractual relationship. (*Global Asset Capital, Inc and Another v Aabar Block S.A.R.L and another* [2017] EWCA Civ 37)

Key lessons

- **Subject to contract wording**: The judgment is a reminder of the importance of expressing preliminary documents and communications to be "subject to contract", and that clear evidence is required to waive a "subject to contract" requirement.

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Company law

There have been some particular cases of interest on a range of company law issues.

Employee share-splitting on a takeover scheme of arrangement

The High Court sanctioned a scheme of arrangement despite "share-splitting" by employees aimed at defeating the scheme on the basis of the "majority in number" requirement.

The court had to decide whether on the facts it was correct to disallow split votes of shareholders opposing the scheme. If those votes were allowed the scheme would have failed, because it would not have been approved by a majority in number of members or the class of members present and voting at the court meeting. This is required under English law as part of the dual test under which that majority in number must also constitute 75% in value of members or each class of the shares voted. S had made a recommended offer for D plc to be effected by scheme of arrangement. In between the directions hearing to convene the court meeting of shareholders to approve the scheme and actually holding that court meeting one employee of D acquired 461 shares. He then gifted one share each to 443 individuals. This more than doubled the number of members on the share register. D obtained a directions order from the court to allow the chairman to exclude the "split" votes at the court meeting. On this basis the vote was passed. At the sanction hearing the High Court sanctioned the scheme, excluding the split votes. The High Court stated that share-splitting undermines the spirit of the schemes legislation. Even without court permission the chairman had a discretion to exclude the split votes to protect the court meeting against manipulation. At a court meeting of a class of members the members must vote in the interests of the class as a whole and not in their own specific interests if different from the interests of the class. Members should fairly represent their class, act in good faith and not coerce a minority to promote interests adverse to the class. The rule in relation to general meetings that a shareholder may vote from motives of individual interest does not apply. There was sufficient evidence for the chairman to have concluded that the new members had joined with the pre-conceived notion of voting down the scheme and so could not have considered the interests of the class. The scheme was very much in the financial interests of members, and an intelligent and honest member of the class who was concerned and acting in respect of his own interest might reasonably approve the scheme. (*Re Dee Valley Group plc* [2017] EWHC 184 (Ch))

Key lessons

- **First share-splitting exercise**: This appears to be the first English case in which share-splitting has been undertaken with the apparent objective of defeating a scheme of arrangement.
- **Buying-in stakes earlier in bid process**: It remains unclear whether the votes on the split shares would have counted if the employees had acquired their stake before the directions hearing to convene the court meeting.
- **"Majority in number" test for scheme threshold**: Whilst the judgment shows that share-splitting did not work here to defeat the scheme, there may be an argument for reform of the headcount test for approving a scheme of arrangement to remove the majority in number requirement. This has already been re-visited in Hong Kong following *Re PCCW, Ltd.*[2]

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Class composition for court meeting to approve a scheme of arrangement and honest intelligent assessment when shares unlisted

The High Court decided that there was one class of shares for the purposes of the court meeting to approve a scheme of arrangement, despite certain shareholders entering into contracts to provide services in exchange for proportionally nominal consideration conditionally on the scheme being sanctioned.

An unlisted company (C) received an unsolicited approach for a takeover to be effected by way of scheme of arrangement. C and its subsidiaries ran the Baltic Exchange. Its board of directors implemented a detailed review of the future of the company and the terms of the takeover with its financial adviser. A single class of ordinary shares was in issue. It was a feature of the Baltic Exchange's operations

Key lessons

- **Minor side deals and related arrangements**: The judgment provides helpful confirmation that minor arrangements should not trigger a need for separate class meetings.

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2 [2009] HKCA 178.

that "panellists" produced or contributed to the freight market indices without formal contractual arrangements with C. It was proposed to formalise these arrangements if the scheme went ahead. Contracts had already been entered into, conditional on the scheme being sanctioned. These provided for free membership of the Baltic Exchange for panellists and continued free access to data. The question was whether this put panellist shareholders into a separate class from other members for the purpose of approving the scheme. The established test is that persons who constitute a class are those whose rights are not so dissimilar as to make it impossible for them to consult together with a view to their common interest. The High Court decided that there was only one class of shares under the scheme which was capable of approval by an intelligent, honest person. The modest annual benefit under the contracts in question (around £7,500 a year) relative to the consideration (£24 million among panellist shareholders holding around 28% of the scheme shares) made it absurd to suggest that the provision of the additional contractual benefits triggered a need for two classes of scheme shareholder. (*Re Baltic Exchange Limited* [2016] EWHC 3391 (Ch))

Directors' duties, transactions at an undervalue and substantial property transactions with directors

The High Court has set aside a series of transactions unauthorised or at an undervalue by a company (C) which later went into liquidation. The transactions contravened a number of UK company and insolvency law requirements and, for the most part, were made against the backdrop of an outstanding group litigation environmental claim against C.

In one transaction C's factory was transferred to its managing director and controlling shareholder (D) and leased back for rent. D alleged that the purchase price was not below market value. However, there was no board resolution authorising the transfer nor explaining why it would promote the success of the company and D did not organise a professional valuation of the property. The High Court ordered D to restore the factory to C and compensate it for the rent. Subsequently, most of C's shares were bought back from D, with the price left outstanding as a secured loan. The High Court decided that the share buyback was equivalent to a distribution to shareholders for no consideration and was liable to be set aside under the UK Insolvency Act, as it amounted to a transaction at an undervalue intended to put assets beyond the reach of creditors. The court said the dominant aim had been to prejudice the interests of environmental claimants. The share buyback was void anyway, because it failed to comply with the UK Companies Act requirement for payment for a buyback to be made on purchase. However, the court decided that D had not been in breach of duty for failing to take into account the interests of creditors when entering into the factory sale. The creditors' interests duty was not triggered just because there was a recognised risk that C might become insolvent in the future (if it lost the litigation), when it was solvent and trading successfully at the time of the sale. Finally, D had not had board authority to acquire a subsidiary of C for £1, when the true value was £214,000. In any event, that had been a substantial property transaction with a director requiring shareholder approval, which had not been obtained, making it voidable. When assessing whether those rules apply you had to look to actual value not the price the director paid. An appeal hearing is awaited in relation to the judgment. (*Dickinson v NAL Realisations (Staffordshire) Ltd. and others* [2017] EWHC 28 (Ch))

Key lessons

- **Full board consideration of undervalue transactions**: Board deliberations to consider proposed transactions at less than market value or with connected persons should consider professional valuations, the company's financial position and whether the transaction will promote the success of the company.
- **Putting assets beyond the reach of creditors**: The judgment clarifies that a share buyback can amount to a "transaction" for the purposes of the UK Insolvency Act rules on transactions at an undervalue with intent to defraud creditors.
- **Creditors' interests duty**: The judgment supports other recent case law that the creditors' interests duty is not engaged just because the company may become insolvent in the future.
- **Substantial property transactions with directors**: The judgment demonstrates that, when assessing whether these rules apply, you look to the true value of the property rather than the transfer price.
- **Payment for share buybacks**: The judgment is a reminder of the UK Companies Act requirement for payment for a buyback to be made on purchase.

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Effect of filing wrong articles of association and meaning of "subsidiary"

The High Court has confirmed that the articles of association of a company are the constitution that the company has resolved by special resolution to adopt and these are what apply as against members, even if incorrect articles are registered.

The issue arose of what share valuation to apply under the articles of a company (C) on a compulsory buyout of the shares of a former employee (G) when he ceased to be employed by C's group. This, in turn, hinged on when G's employing company ceased to qualify as a "subsidiary" within the group. C applied a five times profits valuation when G's shares were compulsorily acquired, which valued the shares at nil although he was in fact offered par value. This approach was based on past changes to the articles adopted by special resolution of C. However, the articles registered at UK Companies House did not reflect these changes and instead provided for a fair valuation method. This would have resulted in a significantly higher sale price. The High Court decided that the five times profits valuation was correct. The court said that the status of correctly adopted articles did not depend on registration, and filing incorrect articles did not give a status to articles incorrectly filed. Any other view would allow companies to circumvent the need to pass a special resolution to amend articles by registering something else. Further where, as here, "subsidiary" was defined in the articles by reference to the statutory definition that was the test you applied. It was irrelevant that at some earlier point C had accounted for G's employing company as a joint venture rather than a subsidiary, and that did not affect the date the compulsory buyback was triggered. You had to apply the statutory definition of "subsidiary" and not UK generally accepted accounting principles. (*Gunewardena v Conran Holdings Limited* [2016] EWHC 2983 (Ch))

Key lessons

- **Registration does not validate an error**: Registration of articles does not sanitise an error in the content of what is filed.
- **Distinction between members and third parties**: Whilst the effect is that members are bound by amendments whether or not registered, the UK Companies Act 2006 specifically states that a company cannot rely on amendments against a third party which have not been registered.

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Past effective date for cross-border merger by absorption of wholly-owned subsidiary

The High Court has confirmed that a past effective date may be given for a merger by absorption of a wholly-owned subsidiary under the Companies (Cross-Border Mergers) Regulations 2007 (Regulations).

The Regulations provide that the draft terms of a merger must specify the date from which the holding of shares or other securities in the transferee will entitle the holders to participate in profits. They also state that the court must not make an order to approve the pre-merger requirements under the Regulations unless this has been complied with. Despite this, the High Court decided that it did not matter that a past effective date had been given for participation in profits in the draft terms of merger for a merger by absorption of a wholly-owned subsidiary. The reason was that there is an express exception in the Regulations from having to give an effective date for participation in profits in the case of that type of merger. The court said that as there was no primary requirement to specify a legal effective time, indicating such a time with a past date did not matter. (*In the matter of iTouch Limited* [2016] EWHC 3448 (Ch))

Key lessons

- **Effective dates in relation to other types of mergers under the Regulations**: It was left open whether giving a past date for participation in profits would work for the other two types of merger under the Regulations, namely, a merger by absorption or a merger by formation of a new company. The exception from specifying an effective date for participation in profits only applies to a merger by absorption of a wholly-owned subsidiary, and so a past effective date may not necessarily work for the other types of merger.

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UK parent did not owe duty of care in relation to operations and property of overseas subsidiaries abroad

Two recent High Court decisions decided on the facts that there was no real issue between the parties as the UK parent company did not owe a duty of care to third parties in relation to the operations or activities on the property of its overseas subsidiaries abroad.

In the first case, a claim was brought against R plc for environmental damage caused by a joint venture operated by its Nigerian subsidiary (S), to which R was not a party. The High Court decided that it was not arguable that R owed a duty of care to the claimants for what had happened. Among other things, it took into account that R did not have a direct shareholding in S, it did not conduct operations in Nigeria and it did not exercise oversight or control there. In the second case the High Court decided that it was not arguable that U Plc owed a duty of care to protect employees and local residents on a tea plantation owned and operated by its Kenyan subsidiary from violence from third parties following a presidential election. The events which had taken place were not foreseeable and a claim that it was fair, just and reasonable to impose a duty was bound to fail. Appeal hearings are awaited in relation to both judgments. (*Okpabi v Royal Dutch Shell and another* [2017] EWHC 89 (TCC) and *AAA and others v Unilever plc and another* [2017] EWHC 371 (QB))

Key lessons

- **Previous test for imposing a duty applied**: These judgments apply the previous test from the Court of Appeal in *Chandler v Cape*[3] as to whether the parent had assumed responsibility to the third party, taking into account whether the damage was foreseeable, there was a sufficient proximity between the parties and it was fair, just and reasonable to impose a duty.

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3 [2012] EWHC Civ 525.

Listed companies

A number of rulings by the English court, the FCA, the Hearings Committee of the Takeover Panel and the Takeover Appeal Board are of particular interest to listed companies.

When identification by name or synonym triggers third party rights for a person "identified" in an FCA Notice

The Supreme Court decided that a person is "identified" in a UK Financial Conduct Authority (FCA) notice, triggering third party rights, if identified by name or synonym (such as office or job title) which could apply to only one person identifiable from information in the notice or publicly available.

M was head of the London division of an investment bank called the Chief Investment Office, which managed the bank's synthetic credit portfolio (SCO). Following significant losses in the SCO division, the FCA reached a regulatory settlement with the bank and served related decision and final notices on the bank in September 2013. The FCA subsequently fined M £736,000 in 2016 for failing to report concerns about the losses, although he was found not to have acted dishonestly. M brought an action that he had been identified in the 2013 final notice served on the bank at a time when the investigation into M's own involvement was ongoing. He alleged this had triggered third party rights under the Financial Services and Markets Act 2000 (FSMA), such as to make representations. M based this claim on the use of the term "CIO London management" in the notice. He suggested that people in his professional sphere would have believed that this referred to him and that, if publicly available information had been read side by side with the FCA notice, his identity could be deduced (focusing on a US Senate Committee report describing his role and identifying him by name). The Supreme Court decided that M had not been identified in the 2013 final notice. The test for identification requires either a name or a synonym, such as office or job title, which only refers to one person and that person is identifiable from the notice or from publicly available information. However, resort to information publicly available elsewhere is only permissible to interpret (as opposed to supplement) the language of the notice. Public information must be freely available and straightforward and simple. This did not include jigsaw identification (such as from the US report) or people "in the know". The relevant audience was the public at large, not a particular sector of the public with special information. (*FCA v Macris* [2017] UKSC 19)

Key lessons

- **Uncertainty over test and application to facts**: It remains to be seen how this test will be applied in practice on different facts.
- **Workability for FCA**: If the test for what amounts to a third party were to become too wide the third party rights would be unworkable for the FCA.

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Mandatory takeover offer at below market price

The UK Takeover Appeal Board (TAB) ruled that a shareholder had acted in concert with others in the acquisition of shares in Rangers International Football Club plc (R), triggering the requirement to make a mandatory cash takeover offer, even though this was now at below market price.

A shareholder (K) and another individual (L) discussed a consortium funding proposal for R and, later, acquiring a possible blocking stake. They subsequently bought shares at 20p per share, taking their collective stake to 19.5%. On the same date K instigated the acquisition of 14.6% of R's shares at the same price by his family trust (N). R's directors were removed, K's nominees appointed and K became chairman. The main question was whether interests in shares carrying more than 30% of the voting rights of R had been acquired by persons acting in concert so as to trigger the requirement to make a mandatory bid. The TAB decided they had. Although 14.6% of the shares were in N's name, K had acted and given instructions as acquirer. He had general control over the 14.6% shareholding in N's name within the meaning of having an "interest in securities" for the purposes of assessing whether Rule 9 was

Key lessons

- **Mandatory offer at below market price**: Mandatory offers are intended to be fundamental to fairness by giving shareholders the chance to sell where control has shifted, but this decision shows that it did not matter whether shareholders would in practice benefit.
- **First use of Takeover Panel's enforcement ability through a court order**: It is the first time the Panel has sought a court order to enforce its powers.

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triggered. The UK Takeover Code is also explicit that a person is deemed to be acting in concert with close relatives and related trusts of any of them. Further, on the facts K and the other individuals had also been acting in concert. The definition of acting in concert is wide and catches tacit understandings as well as nods and winks. Direct evidence is rare, but the co-operation on the proposed capital injection and blocking stake here, as well as evidence from email correspondence, were overwhelming. As the principal member of the concert group K had to make a mandatory offer at the 20p acquisition price. It did not matter that R's share price now exceeded 20p and there was no financial benefit to shareholders. This is the first case in which the UK Takeover Panel has sought to use its right to obtain a court order to enforce its powers (here, to compel the mandatory offer). (*Takeover Appeal Board 2017/1 and Panel Statement 2017/8*)

Flagrant and systemic dishonesty in dealing with Takeover Panel resulted in "cold shoulder"

The Hearings Committee of the UK Takeover Panel has "cold shouldered" two individuals who intentionally provided inaccurate information to a Panel investigation, with the effect that regulated firms cannot act for them on transactions to which the UK Takeover Code applies.

Until 2013 M and his family believed that they owned just under 30% of H plc (H), a company traded on NEX (previously PLUS and then ISDX). That year a company owned by M bought shares in H which would have put the combined holding over 30% of the voting rights, triggering the requirement to make a mandatory offer under Rule 9 of the Code. M's broker discovered this in 2015 and advised M to consult the Takeover Panel. M alleged that the additional shares were acquired on behalf of his family friend G and failed to contact the Panel. M and G signed a promissory note in 2015 to ratify the arrangement, backdating it to 2013, and M bought shares in a company owned by G of a comparable price to the additional shares in H. The Panel launched an investigation. It transpired that M's family holding in H had been 50% throughout, meaning a mandatory offer was not in fact required. However, the Hearings Committee decided that M and G had failed to deal with the Panel in an open and co-operative way as required by the Code. It ruled that M and G had invented the arrangement and fabricated evidence. M was cold shouldered for six years, taking into account that he had been privately censured twice previously (including once for not dealing with the Panel in an open and co-operative manner) and publicly censured once before (for failing to comply with Rule 9). G was cold shouldered for two years. (*Morton and Garner Takeover Panel Hearings Committee 2017/1*)

Key lessons

- **Honesty and openness needed to regulate the conduct of takeovers**: Following the broker's advice and open consultation with the Panel would have resolved the matter.
- **Consequences of failing to identify concert parties**: Failing to identify concert parties may result in inadvertent breach of the requirement to make a mandatory offer.

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Redress scheme to compensate investors for market abuse

The FCA has used its power to require compensation to be paid to the investors in a listed company for the first time, for a false trading update.

In August 2014 T plc issued a trading update with inflated expected trading profit. A month later T announced it had identified an overstatement of expected profit. The total overstatement was £284 million. Under the applicable FSMA regime at the time market abuse was the giving of a false or misleading impression by a person who could be reasonably expected to know it was false or misleading. On the facts the relevant knowledge was not at board level but was nonetheless known at the level of finance director, commercial director and managing director. The FCA decided that the market abuse was known at

Key lessons

- **Restitution**: This is the first time the FCA has exercised its discretion to require restitution for market abuse.
- **Lack of interviews and witness statements by T**: This type of co-operation by companies may in practice reduce their ability to strengthen their systems and controls.

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a sufficiently high level to constitute T's knowledge. It had resulted in a false market in which, until corrected in September 2014, buyers of securities had paid more than they should have. The FCA issued a public censure and, for the first time, exercised its discretion to require restitution by T to investors who had overpaid for securities. The FCA indicated that it expected this would amount to around £85m plus interest. It did not impose a penalty as a separate deferred prosecution agreement with the SFO had imposed a £129 million fine. The FCA also took into account T's exemplary co-operation and steps it had taken to prevent future market abuse. Co-operation included not interviewing witnesses or taking statements but, rather, voluntarily disclosing material appearing significant. (*Tesco plc, FCA Final Notice* 28 March 2017)

Good faith

An interesting decision has looked at duties of good faith.

No implied term of good faith regarding termination of distributorship agreement

The Court of Appeal decided that a principal was entitled to terminate a distributorship agreement on six months' notice on the wording of the contract, and that no implied duty of good faith applied when invoking the termination provisions.

One clause in the distributorship agreement allowed termination by either party on six months' notice after an initial period of three years. Another allowed the principal (P) to terminate on three months' notice if dissatisfied with performance of the distributor (D), provided D was first given the chance to remedy the breach. D alleged that it had invested money on the basis of a variation by conduct which precluded termination for several further years. It also argued that P had not warned it of concerns over performance and that a term should be implied that it would do so and, more broadly, that one party would give the other appraisals of the prospect of the relationship continuing and not give the other party a misleading impression of those prospects before terminating. The Court of Appeal denied this. It decided that P was entitled to terminate simply on six months' notice after the initial term, even if dissatisfied with D's performance. Requiring appraisals would have introduced an entirely new concept into the contract, and a requirement not to give a misleading impression was unnecessary and hopelessly vague. In any event, there was no arguable case of conduct that lacked good faith and it would be inappropriate to introduce requirements for communication and co-operation in relation to termination provisions. (*Sirketi and Sirketi v Perkins Engines Company Limited* [2017] EWCA Civ 183)

Key lessons

- **Good faith provisions in long-term relational agreements reined in**: Recent case law has in any event cast doubt on earlier decisions to imply a duty of good faith into a long-term relational agreement. This judgment now suggests that, in any event, it would be inappropriate to imply such a term in relation to a termination provision.

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