Bond Repurchases – an Issuer's Guide to Questions to Ask and Points to Consider

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Authors: Jill Concannon, Rob Mathews, James Greene, Colin Chang, Gary Kashar, Jonathan Michels, Tommaso Tosi

In the current environment, issuers may start to consider whether, if their bonds are trading at a discount to par (or may be in the future), they should repurchase their bonds. The White & Case leveraged finance team puts forward these key points to consider when planning a bond repurchase transaction.

The Basics

A bond repurchase, or bond buyback, refers to the process whereby the issuer approaches the open market and repurchases its bonds from holders. If the bonds are trading at less than their par value, issuers can use this tool opportunistically to reduce their overall interest expense. Although there are other liability management processes issuers can use to reduce their outstanding indebtedness (for example, a tender offer), repurchases are advantageous for issuers that wish to capitalise relatively quickly on a depressed market price for their bonds. One benefit of bond repurchases is that they do not require legally mandated time periods (for example, tender offers for bonds in the US are, with limited exceptions, required to remain open for 20 business days) or offering documentation.

Creeping Tenders

When structuring your bond repurchase program, you must ensure that you are not conducting what is, under US securities law, essentially a tender offer by another name; otherwise, you would risk being in violation of US tender offer rules if your repurchase program targets US holders. Even small repurchases can, in some circumstances, be grouped together in a way that violates the tender offer rules. Although these rules regulate tender offers, they, somewhat unhelpfully, do not define what a tender offer is. So US courts have stepped into the void, setting forth various factual tests to determine whether or not a securities repurchase program is actually a tender offer.

The most prominent among these tests are the so-called "Wellman" factors (as developed in *Wellman v. Dickinson*, 475 F. Supp. 783, 823-824 (S.D.N.Y. 1979)), which are weighed when making this determination. Under this test, your bond repurchase program could be seen to be a tender offer if at least some of the following statements about it are true:

- the offer is disseminated in a widespread manner to the market, for example by press release;
- a premium to the market price is offered;
- there is no meaningful opportunity to negotiate price or terms of the offer (it is effectively "take it or leave it");

- the offer is for a substantial percentage of the outstanding issue;
- the offer is contingent on a minimum principal amount of bonds being tendered;
- the offer is open for only a limited period of time;
- recipients of the offer are under pressure to respond to the offer; and
- the announcement of an acquisition program has been followed by a rapid accumulation of bonds.

The factors are effectively an attempt to distil the traditional features of a tender offer—*i.e.*, if it looks like a tender offer and smells like a tender offer, it is one.

Avoiding a tender offer

We would recommend a few common-sense steps to avoid your bond repurchases being considered tender offers in disguise:

- Instruct a limited number of banks to make enquiries on your behalf. Engaging one or two brokers who understand the above limitations and what you are trying to do will ensure things are coordinated.
- Ensure that your banks reach out to a limited number of investors. If these are 144A high yield bonds, they are likely to still only be held by institutional investors. Even so, your banks should make calls to a limited number of institutions that they know are likely to be holding the bonds (versus a Bloomberg or other similar communication sent to the entire market).
- Conduct the offers over a reasonable period of time and avoid coercive behaviour and pressure. Think private, individually negotiated transactions rather than "take it or leave it" behaviour.
- Control the size of the repurchase. The repurchase program should not be for the entire series of the notes or a substantial percentage (more on this below).

We are also asked from time to time whether it is possible to launch a tender offer after doing some repurchases. Care should be taken to ensure that no decision has been made to commence a tender offer while repurchases are being made, so a decision to conduct a tender offer and any preparations for a tender offer should start only after the repurchase program is finished.

25% rule? Maybe (or maybe not)

Market participants often cite the "25%" rule for determining the threshold of what is considered a "substantial percentage" of a particular class of notes—meaning that you are relatively safe below 25%. The "25%" rule comes from US case law (*Hanson Trust PLC v. SMC Corporation*, 774 F. 2d 47 (2nd Cir. NY 1985)), where the court found that a combination of privately negotiated and open market repurchases of equity securities totalling less than 25% of the total outstanding securities did not constitute a tender offer. Some practitioners in the market take the view that this "25%" rule may not necessarily apply to repurchases of debt securities, because the context and potential effect of a debt repurchase versus an equity repurchase are different. We believe that it is still a reasonable rule of thumb to follow, particularly given disclosure obligations (see below), which may dictate that you disclose purchases above a particular threshold where they are considered material, although the analysis should be done on a case-by-case basis based on context, facts and circumstances.

Disclosure to the market

We are frequently asked whether bond repurchase programs need to be disclosed (and when).

If you are subject to the Market Abuse Regulation ("MAR"), the general rule is that issuers must inform the public as soon as possible of inside information which directly concerns the issuer. Any buyback of a significant percentage of an outstanding bond issue that, if made public, would have a significant effect on their price, or on the price of related derivative financial instruments, would constitute inside information.

Your investment bank should be consulted to ensure that the amount of the outstanding issue that you propose to repurchase would not be considered price-sensitive (or that the buyback is not price-sensitive for other reasons, such as reducing the overall cash position of the issuer as a result of the buyback).

If MAR does not apply to you as an issuer, a reference to the repurchase program should generally be made to bondholders in the next interim or annual report. You should also consider whether the stock exchange where the bonds trade would require disclosure. As a general rule, they do not require prior disclosure as long as the repurchase is not material and is otherwise permitted by the bond documentation.

What do you know?

It may go without saying, but when you approach the market and make repurchases, you should be sure that any material non-public information has been released (and avoid making repurchases until you have done so).

We recommend that any closed periods that issuers already have in place for, for example, management sales of securities be observed (including trading "windows" observed before the release of results and immediately thereafter). If you have no official windows in place, you should avoid being in the market for a reasonable period before your interim or annual results are made public. Each "window" is reasonably fact-specific and dependent on how information typically crystallises before each report (for example, a company with far-flung operations that take a long time to consolidate may be comfortable that their results come together quite close to a reporting date, whereas companies that have fewer jurisdictions or tighter controls may be more sure of their results earlier).

What does the indenture (or other relevant documentation) say?

European high yield bond indentures typically permit voluntary repurchases of bonds with no limit (and sometimes affirmatively include a statement to the effect that they are permitted). This is also usually expressly stated in the offering memorandum related to issuance of the bonds.

Restricted payments covenants in indentures will treat repurchases of "subordinated" indebtedness (traditionally, contractually subordinated debt only—*i.e.*, not indebtedness that is structurally junior or unsecured) as a restricted payment. It is also worth noting that under a typical indenture, if you repurchase notes and cancel them, you (unlike in a simultaneous refinancing) may lose capacity to re-incur the debt.

You should also confirm that your senior credit facility, if any, does not restrict or limit repurchases of other indebtedness.

To cancel/not to cancel

European bond indentures typically do not require notes acquired to be cancelled (they may be held in treasury indefinitely). However, typically any notes held by the issuer or any of its affiliates are, under the terms of the notes, no longer considered outstanding for voting purposes (and thus cannot be voted by the issuer or its affiliates in a consent solicitation or a waiver process, for example).

Tax

As with any transaction, issuers should consult their tax advisers to confirm the tax treatment of the proposed repurchase and when any gain will be recognised for income tax purposes.

EMEA leveraged finance partners

David Becker ●
Partner, London
T +44 20 7532 1405
E dbecker@whitecase.com

Paul Clews ●
Partner, London
T +44 20 7532 1436
E paul.clews@whitecase.com

Jill Concannon ●
Partner, London
T +44 20 7532 1534
E jconcannon@whitecase.com

Lee Cullinane ■
Partner, London
T +44 20 7532 1409
E lcullinane@whitecase.com

Chris Czarnocki ■
Partner, London
T +44 20 7532 1201
E cczarnocki@whitecase.com

Jeremy Duffy ■
Partner, London
T +44 20 7532 1237
E jduffy@whitecase.com

Gareth Eagles ■ ●
Partner, London
T +44 20 7532 1251
E geagles@whitecase.com

Jacqueline Evans ■
Partner, London
T +44 20 7532 1404
E jevans@whitecase.com

Martin Forbes ■
Partner, London
T +44 20 7532 1229
E martin.forbes@whitecase.com

Emma Foster ■
Partner, London
T +44 20 7532 1299
E efoster@whitecase.com

James Greene ■ ●
Partner, London
T +44 20 7532 1439
E jgreene@whitecase.com

James Hardy ■
Partner, London
T +44 20 7532 2728
E james.hardy@whitecase.com

Colin Harley ■
Partner, London
T +44 20 7532 1200
E colin.harley@whitecase.com

Rob Mathews ●
Partner, London
T +44 20 7532 1429
E rmathews@whitecase.com

Shane McDonald ■
Partner, London
T + 44 20 7532 2698
E shane.mcdonald@whitecase.com

Jeffrey Rubinoff ■
Partner, London
T +44 20 7532 2514
E jeffrey.rubinoff@whitecase.com

Justin Wagstaff ●
Partner, London
T +1 212 819 2694
E jwagstaff@whitecase.com

Ben Wilkinson ■
Partner, London
T +44 20 7532 1276
E ben.wilkinson@whitecase.com

Thierry Bosly
Partner, Brussels
T +32 2 2392 509
E tbosly@whitecase.com

Hadrien Servais ●
Local Partner, Brussels
T +32 2 2392 544
E hadrien.servais@whitecase.com

Claire Matheson Kirton ■
Partner, Dubai
T +971 4 381 6218
E cmathesonkirton@whitecase.com

Rebecca Emory ●
Partner, Frankfurt
T +49 69 29994 1432
E rebecca.emory@whitecase.com

Thomas Flatten
Partner, Frankfurt
T +49 69 29994 1233
E tflatten@whitecase.com

Giles Teerlinck ■ ●
Partner, London
T +44 20 7532 2232
E giles.teerlinck@whitecase.com

Florian Degenhardt
Partner, Hamburg
T +49 40 35005 298
E fdegenhardt@whitecase.com

Vanessa Schuermann ■
Partner, Frankfurt
T +49 69 29994 1431
E vanessa.
schuermann@whitecase.com

Gernot Wagner ●
Partner, Frankfurt
T +49 69 29994 1430
E gernot.wagner@whitecase.com

Tanja Törnkvist
Partner, Helsinki
T +358 9 228 64 351
E ttornkvist@whitecase.com

Güniz Gökçe
Partner, Istanbul
T +90 212 355 1311
E guniz.gokce@gkcpartners.com

Yoko Takagi
Partner, Madrid
T +34 91 7876 320
E yoko.takagi@whitecase.com

Iacopo Canino
Partner, Milan
T +39 02 00688 340
E icanino@whitecase.com

Gianluca Fanti
Partner, Milan
T +39 02 00688 390
E gianluca.fanti@whitecase.com

Michael Immordino ●
Partner, Milan, London
T +39 020 068 8310
T +44 20 7532 1399
E mimmordino@whitecase.com

Alessandro Nolet ■
Partner, Milan, Hong Kong
T +39 020 068 8420
T +852 2822 0411
E anolet@whitecase.com

Natalia Nikitina
Partner, Moscow
T +7 495 787 3027
E nnikitina@whitecase.com

Samir Berlat
Partner, Paris
T +33 1 5504 1551
E samir.berlat@whitecase.com

Colin Chang ●
Partner, Paris
T +33 1 5504 5815
E cchang@whitecase.com

Denise Diallo ●
Partner, Paris
T +33 1 5504 1518
E ddiallo@whitecase.com

Raphaël Richard
Partner, Paris
T +33 1 5504 1538
E rrichard@whitecase.com

Jan Linda
Partner, Prague
T +420 255 771 271
E jlinda@whitecase.com

David Plch
Partner, Prague
T +420 255 771 298
E dplch@whitecase.com

Jonathan Weinberg ■
Partner, Prague
T +420 255 771 262
E jweinberg@whitecase.com

Oscar Liljeson
Partner, Stockholm
T +46 8 50632 379
E oscar.liljeson@whitecase.com

Carl Hugo Parment
Partner, Stockholm
T +46 8 50632 341
E carlhugo.parment@whitecase.com

Magnus Wennerhorn
Partner, Stockholm
T +46 8 50632 370
E magnus.wennerhorn@whitecase.com

Nicholas Coddington ■
Local Partner, Warsaw
T +48 22 5050 160
E ncoddington@whitecase.com

Tomasz Ostrowski ■
Partner, Warsaw
T +48 22 5050 123
E tostrowski@whitecase.com

■ English Qualified ● US Qualified

White & Case LLP
5 Old Broad Street
London EC2N 1DW
United Kingdom

T +44 20 7532 1000

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