C/M/S/ Cameron McKenna

The Companies Act 2006

Takeovers and electronic communications - update

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On 8 November 2006 the Companies Bill finally became the Companies Act 2006. Eventually the new Act will repeal and replace nearly all of the Companies Act 1985 and:

- simplify the administrative burden on smaller private companies, which make up the vast majority of the corporate population;
- facilitate shareholder engagement, particularly in quoted companies; and
- update and clarify the law in various areas, particularly in relation to directors' duties.

Only a handful of the Act's 1,200-odd sections and 16 Schedules came into force at the time of Royal Assent. The Government has said that the remaining parts will all be in force by **1 October 2008**.

This article looks at two of the most important parts of the Act: the provisions relating to takeovers, which will come into force on 6 April 2007; and those relating to electronic communications between companies and their shareholders, which will come into force **on 20 January 2007**.

For an overview of the whole Act, see our article "The Companies Act 2006: deferred reform", which can be found by **clicking here**.

Banks and other lenders can find details of those provisions of the Act which will particularly affect them in our article entitled "The Companies Act 2006: issues for lenders", which can be found by **clicking here**.

TAKEOVERS

Changes to the squeeze-out procedure

Although it is rare for a minority shareholder to challenge a bidder's right to acquire his shares compulsorily under sections 428-430F of the 1985 Act, in fact there are a number of traps which, if a bidder falls into one of them, could result in its compulsory acquisition being declared invalid. For example:

- It is normally of vital importance to a bidder to be able to count shares that it has been promised under an irrevocable undertaking towards the 90% threshold for effecting the squeeze-out. Section 428(5) allows this, provided that the irrevocable is given by the registered holder of the shares and the bidder does not give any consideration other than a promise to make the offer. In practice, where shares are held by a nominee on behalf of a pension fund or other institution, it may not be possible to get the registered holder to give the irrevocable, and the bidder will have to rely on one signed by, say, the fund manager.
- There can also be difficulties under the current rules where the offer includes shares "to be issued" pursuant to the exercise of options or convertibles, so that in the fraction to calculate whether the bidder has acquired 90% of the shares to which the offer relates the denominator will vary according to the number of shares that are actually issued after the offer document is posted (creating a "floating threshold"). Similarly, if options are exercised after the deadline for sending squeeze-out notices has passed, the bidder cannot acquire the resulting shares.

Several years ago the Company Law Review Steering Group recommended that these and other problems should be ironed out. In particular, the existing provisions were found to be ambiguous as to whether shares should count as shares the bidder has contracted to acquire where it has contracted conditionally; and it was felt that legislative sanction should be given to the long-standing but legally uncertain practice of extending an offer to certain overseas shareholders by putting an advert in the UK edition of the Financial Times.

When the Takeovers Directive (Interim Implementation) Regulations were introduced in May this year, they applied a new squeeze-out mechanism to takeovers of companies whose shares are traded on an EU regulated market. As a result, for takeovers of companies within the scope of the Directive, the Regulations dealt with the issue of conditionally acquired shares, and allowed a bidder to extend its offer to overseas shareholders by placing a notice in the Gazette and making the offer document available for inspection at a place in an EEA state or on a website. But, as the Secretary of State's power to make the Regulations extended only to implementing the Takeovers Directive, the Regulations did not clear up the other problems, or apply to takeovers that fell beyond the scope of the Directive. These the Government promised to deal with in the 2006 Act.

The rules in the new Act are therefore designed principally to apply the changes introduced in May to takeovers of all UK companies (whether or not within the scope of the Directive), and to remove the remaining traps, in order to make it easier for a bidder to operate the squeeze-out machinery safely. In particular:

- as long as the giver of an irrevocable intends "to secure that the [legal] holder will accept the offer when it is made", under the new provisions the shares can be counted towards the 90% threshold;
- where the offer includes shares "to be issued" pursuant to the exercise of options or convertibles, in calculating whether it has acquired 90% of the shares to which the offer relates the bidder will be able to "freeze" the denominator at the number of shares that are actually in issue at the time it proposes to initiate the squeeze-out;
- in most takeovers there will be no effective deadline for the bidder to send squeeze-out notices, so even if option-holders exercise their options to acquire target shares late in the day, a bidder should be able to acquire their shares compulsorily;
- if a minority shareholder wishes to challenge the compulsory acquisition of his shares by applying for a court order, he will have to notify the bidder of his application, and in turn the bidder must notify all the other minority shareholders that proceedings have been started. At present there are no such obligations, and it can be difficult for a bidder to discover whether any shareholder has objected to the squeeze-out.

Sections 428-430F of the 1985 Act, and the Interim Regulations, will be repealed.

Takeover Panel

The new Act will extend the Takeover Panel's statutory powers to cover all takeovers, rather than only those within the scope of the EC Takeovers Directive, and implement permanently various other provisions of the Directive - replacing the interim arrangements that were put in place on 20 May this year to meet the Directive's deadline. (These were discussed in our article entitled "Changes to the UK takeovers regime on 20 May", which can be found by **clicking here**.)

ELECTRONIC COMMUNICATIONS

Cost-saving

Provisions in the Companies Act 2006 are designed to make it easier for companies to use the internet to communicate with shareholders and debenture-holders. Commencement of the relevant sections has been brought forward to January 2007 in order to enable companies to save printing and distribution costs as early as possible.

Under the 1985 Act, a company can already send notices of meetings and copies of the annual reports and accounts to a shareholder electronically, but only by express agreement with that shareholder. Although it also covers other methods, such as telephoning or sending audio tapes or disks by post, in most cases communicating information electronically means either sending it by e-mail, or notifying intended recipients that it has been published on a website.

The new Act does not specify (and therefore does not limit) the nature of the documents or information that may be sent or received electronically. For all the methods of electronic delivery by a company apart from the website method, the position is like the present regime in that the recipient must have agreed in advance, supplied his electronic address, and not revoked the agreement. There is some relaxation of this in relation to corporate recipients, whose consent to receive electronic communications (in particular, for proxy appointments) is deemed to have been given in relation to any meeting where the notice of that meeting or an instrument of proxy contains the company's electronic address. It will also generally no longer be necessary to make use of enabling provisions for electronic communications in a company's articles (or those in Table A, which all companies are entitled to use whether they have adopted the provisions or not), although shareholder sanction, which is required for website delivery (see below), may be embodied in the articles.

The most significant change under the new Act, however, is that there is a separate and more liberal regime for publication of information on a website, under which companies will be able to assume agreement by recipients unless they hear to the contrary. With the increasing size and sophistication of annual reports in recent years (partly as the result of greater regulation), the opportunity to reduce the print-run offers substantial savings, particularly for publicly quoted companies. Website delivery is likely to become the norm for these companies.

Website delivery by the company

A shareholder may be taken to have agreed to website delivery in place of hardcopy documents where:

- the company has been authorised, either by appropriate provisions in its articles or by a resolution of its members, to send or supply documents or information to members by making them available on a website; and
- the shareholder has either expressly agreed, or is deemed to have agreed, to receive information in this way. Agreement will be deemed to have been given where the company has sent the shareholder a written request (which must clearly setting out the consequences of a failure to respond) to agree to website delivery and the shareholder has not responded within 28 days.

Similar rules apply to communications made to holders of debt securities and debenture holders.

The company must notify the intended recipient that the information is available on its website, and how to access it. The information is not deemed to have been received until notice has been received, or, if later, when the information is displayed on the website (if, for example, the notification is given in advance). Notification will need to be done by post (in which case it will be deemed to have been received 48 hours after posting, or such other period as the company's articles or the debt security instrument may prescribe) unless the recipient has agreed to receive e-mail or another form of electronic delivery and has supplied an appropriate address. The information must remain on the website for whatever period is prescribed by the Companies Acts or, if no period is prescribed, 28 days from the sending of the notice; if the website crashes, the company will not be in default if the information was available for at least part of the period and the failure was through no fault that the company could reasonably have been expected to prevent.

If the recipient of a request to accept website delivery objects within the 28 days, the company will have to continue to send him hardcopies for at least the next 12 months, since it is not permitted to send him another request before then. Those who have not objected in time will still have the right, once they have received information electronically, to insist that the company send a hardcopy, free of charge, within 21 days, but their doing so will not prevent the company from using website delivery on the next occasion. The provisions do, however, appear to contemplate that those who are deemed to have agreed to website delivery (like those who have actually agreed) may revoke that agreement, although there is no prescribed way of doing this.

Listed companies

Listed companies will have to comply with the new Disclosure and Transparency Rules (DTRs), which are coming into effect on 20 January 2007. These reflect the implementation in the UK of the Transparency Directive and largely copy out sections of the Directive, some of which deal with electronic communications.

The DTRs will reflect the Directive in requiring that, where listed issuers wish to send information to holders of shares or debt securities by any electronic means, the decision to do so must be taken in general meeting, and the holders must have been individually requested in writing to consent to the use of electronic means (although their consent is to be assumed unless they have objected within a reasonable time). In other words, in contrast to the position under the Act:

- even companies wishing to use an alternative electronic means to website delivery will require shareholder or debenture-holder approval in addition to individual holders' consent; and
- having appropriate provisions in the articles or the instrument will not necessary be an adequate alternative to obtaining this approval.

The Financial Services Authority is due to publish a special edition of its newsletter, List!, providing guidance on interpreting the DTRs. It is expected, for example, that the FSA will confirm that the 28-day period prescribed under the Act for deemed agreement to website delivery will satisfy the DTR requirement to allow a reasonable time for objection, and that it will only be necessary to send the requests to registered holders.

The DTRs will require that the use of electronic means must not depend on the recipient's location: in other words, the listed company will not be able arbitrarily to decide that holders in certain territories will not be eligible for a particular electronic communication (for example, because the company is concerned to avoid regulatory reasons in those territories). To avoid being in default of the DTRs, it will have to resort to non-electronic means for all recipients of the communication.

Guidance for existing companies on taking advantage of the new rules

The DTI has told us that it is still considering how the new rules on electronic communications should apply to existing companies whose articles permit certain information to be sent to shareholders electronically. Guidance is expected to be published shortly by the DTI clarifying, for example, whether and how such companies will need to amend their articles to take in the broader scope of the new Act, and whether existing agreements on electronic communication will need to be renewed.

In the meantime, companies will want to consider whether their articles contain anything inconsistent with their ability to take advantage of the new regime, and what, if any, changes they should make in the light of the DTI guidance, once it appears. Listed companies may have to put a resolution to shareholders in any event. Companies should also be thinking of including requests to agree to website delivery in their next posting.

For further information, please contact

Peter Bateman at peter.bateman@cms-cmck.com or on +44 (0)20 7367 3145

Simon Howley at simon.howley@cms-cmck.com or on +44 (0)20 7367 3566

C/M/S/ Cameron McKenna

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CMS Cameron McKenna LLP
Mitre House
160 Aldersgate Street
London EC1A 4DD

T +44 (0)20 7367 3000
F +44 (0)20 7367 2000