

PRACTICE STATEMENT 5

RULE 13.5 – INVOKING CONDITIONS AND PRE-CONDITIONS

1. Introduction

- 1.1 This Practice Statement describes the way in which the Panel Executive normally interprets and applies Rule 13.5(a) of the Takeover Code in relation to when an offeror may invoke a condition or pre-condition to an offer so as to cause the offer not to proceed, to lapse or to be withdrawn.
- 1.2 Rule 13.5(a) was originally introduced as a counterbalance to the widespread use of broadly drafted general protective conditions and addresses the concern this created by requiring an overriding standard of materiality to be satisfied before an offeror can invoke a condition to which the rule applies.
- 1.3 Where a condition is subject to Rule 13.5(a), the offeror may only invoke the condition with the Panel’s consent, which will normally only be given if the circumstances which give rise to the right to invoke the condition are of material significance to the offeror in the context of the offer. This is referred to as the “material significance requirement”.
- 1.4 In this Practice Statement:
 - (a) section 2 categorises the various types of condition to an offer and explains the application of Rule 13.5(a) to those categories;
 - (b) section 3 sets out the Executive’s approach to the invocation of conditions and the factors it will take into account in determining whether the material significance requirement has been satisfied in relation to different categories of condition;
 - (c) section 4 explains that the test for suspending the offer timetable under Rule 31.4(a) is not the same as the test for invoking a condition to an offer under Rule 13.5(a); and
 - (d) section 5 provides guidance as to when a contractual offer or a scheme of arrangement will be permitted to lapse on its long-stop date.

2. Conditions to offers and invoking conditions

(a) Subjectivity of conditions

- 2.1 Rule 13.1 provides that:
 - (a) an offer must not normally be subject to conditions which depend solely on subjective judgements by the board of the offeror or the offeree company or the fulfilment of which is in their hands; but

- (b) an element of subjectivity may be acceptable in certain circumstances, for example, in relation to official authorisations or regulatory clearances.

(b) Material significance requirement

2.2 Where a condition is subject to Rule 13.5(a):

- (a) an offeror may only invoke the condition so as to cause the offer not to proceed, to lapse or to be withdrawn with the consent of the Panel;
- (b) the Panel will normally only give its consent if the circumstances which give rise to the right to invoke the condition are of material significance to the offeror in the context of the offer (i.e. the material significance requirement is satisfied); and
- (c) whether the material significance requirement has been satisfied will be judged by reference to the facts of the case at the time that the relevant circumstances arise.

(c) Categorisation of conditions

2.3 In a typical offer, the conditions can be broken down into six broad categories, as follows:

- (a) Category 1 - conditions relating to the acceptance or approval of the offer by the offeree company's shareholders or the court, i.e.:
 - (i) in the case of a contractual offer, the acceptance condition (i.e. the minimum required level of shareholder acceptance of the offer); and
 - (ii) in the case of a scheme of arrangement, a condition relating to the approval of the scheme by the offeree company's shareholders and a condition relating to the sanctioning of the scheme by the court.
- (b) Category 2 - conditions giving effect to certain requirements of law, regulation or the offeror's articles of association (or equivalent), e.g.:
 - (i) where securities are offered as consideration, or are proposed to be issued to finance cash consideration, a condition required to give effect to a legal or regulatory requirement relating to the issuance, listing and/or admission to trading of those securities; and

- (ii) a condition required to give effect to a legal or regulatory requirement, or a requirement of the offeror's articles of association, for the offeror's shareholders to approve the implementation of the offer.
- (c) Category 3 - in relation to long-stop dates and so-called "mini-long-stop dates":
 - (i) a term relating to the long-stop date of a contractual offer; and
 - (ii) a condition relating to the long-stop date of a scheme of arrangement or a specific date by which the shareholder meetings or the court sanction hearing must be held.
- (d) Category 4 - bespoke conditions relating to the (non-)occurrence of a specific event or circumstances in relation to the offeree company.
- (e) Category 5 - specific or general conditions relating to the obtaining of an official authorisation or regulatory clearance (including conditions relating to there being no "phase 2" reference or similar process).
- (f) Category 6 - other conditions, principally general protective conditions (including a "material adverse change" condition).

(d) Application of Rule 13.5(a) to different categories of condition

- 2.4 A Category 1 or Category 2 condition is not subject to Rule 13.5(a) (see Rules 13.5(b)(i) to (v)). If a Category 1 or Category 2 condition is not satisfied, the offeror will therefore not require the Panel's consent to invoke the condition and lapse the offer.
- 2.5 A Category 3 condition is also not subject to Rule 13.5(a) (see Rules 13.5(b)(vi) and (vii)). Separate requirements apply, however, where it is proposed that a contractual offer or scheme of arrangement will lapse on its long-stop date, as explained in section 5 below.
- 2.6 Category 4, Category 5 and Category 6 conditions are subject to Rule 13.5(a). However, under Rule 13.5(b)(viii), the Panel may agree that any condition (normally a Category 4 condition) will not be subject to Rule 13.5(a) in the particular circumstances. Examples of such conditions (which will normally be non-waivable) include:
- (a) a condition relating to the approval by offeree company shareholders of a transaction under Note 2 on Rule 16.1 (such as a proposed disposal of offeree company assets by the offeror to

a shareholder in the offeree company) or of certain management incentivisation arrangements falling under Rule 16.2; or

- (b) a condition relating to an action by shareholders in the offeree company, such as the rejection of an acquisition or disposal proposed by the offeree board (see Rule 21.1).

3. The Executive's approach to the invocation of conditions

(a) Introduction

3.1 If a condition to which Rule 13.5(a) applies is not satisfied or waived, the offeror must seek the consent of the Executive to invoke the condition so as to cause the offer to lapse. In such circumstances, the Executive will need to consider:

- (a) whether the condition is engaged in accordance with its terms (such that it is capable of being invoked); and, if so
- (b) whether the circumstances which give rise to the right to invoke the condition satisfy the material significance requirement.

3.2 The factors which the Executive will take into account in reaching its determination include those set out in section 3(b). Whilst an offeror may wish to take steps to ensure that as many factors as possible will be satisfied or weigh in its favour, it is not necessary for all relevant factors to be supportive in order for an offeror to be permitted to invoke a condition. The factors are not a "checklist" of items which must all be present for the Executive to give its consent and it is recognised that the satisfaction of one factor may preclude the satisfaction of another.

3.3 The Executive expects to be consulted at the earliest opportunity if an offeror may wish to invoke a condition. The Executive will then establish a reasonable and limited period of time within which the offeror must decide whether it wishes to seek the Executive's consent to the invocation of the condition.

(b) Factors to be taken into account

(i) All relevant conditions

3.4 The Executive will take all relevant factors into account when considering whether the material significance requirement has been satisfied such that it should consent to a request by an offeror to invoke a condition.

3.5 Relevant factors include the following:

- (a) whether the condition was included to take account of the particular circumstances of the offeree company;
- (b) whether the condition was the subject of negotiation with the offeree board;
- (c) whether the condition was expressly drawn to the attention of offeree company shareholders in the offer document or firm offer announcement, with a clear explanation of the circumstances which might give rise to the right to invoke the condition;
- (d) whether the circumstances that have arisen could have reasonably been foreseen at the time of the firm offer announcement and, if they could, the likelihood of the circumstances arising;
- (e) the actions taken by the offeror since the firm offer announcement and, in particular, since the circumstances on which the offeror is seeking to rely arose. For example, if, since the relevant circumstances arose, the offeror has purchased shares in the offeree company, or has made statements indicating an intention to continue to pursue the offer, the Executive will be less likely to agree that the material significance requirement has been satisfied; and
- (f) the views of the offeree board, i.e. the Executive will be more likely to consent to a request by an offeror to invoke a condition if the offeree board agrees that this is the appropriate course of action.

(ii) *General protective conditions, including a material adverse change condition*

- 3.6 The application of Rule 13.5(a) to a general protective condition was considered by the Panel on appeal during the offer for Tempus Group plc by WPP Group plc (see Panel Statement 2001/15), in which the offeror sought to invoke a material adverse change condition.
- 3.7 The Panel concluded that the material significance requirement was not satisfied and stated that "... meeting this test requires an adverse change of very considerable significance striking at the heart of the purpose of the transaction in question, analogous ... to something that would justify frustration of a legal contract."
- 3.8 In applying Rule 13.5(a) in the light of that decision, the Executive's practice is that:
- (a) in the case of a Category 6 condition, in order for the material significance requirement to be satisfied, the offeror will need to demonstrate that the relevant circumstances are of very

considerable significance striking at the heart of the purpose of the transaction; and

- (b) whilst this is a high standard, it does not require the offeror to demonstrate frustration in the legal sense.

(iii) Phase 2 Reference Conditions

3.9 An offeror may include a condition to its offer (a “Phase 2 Reference Condition”) relating to there being no phase 2 reference by the Competition and Markets Authority and/or no “phase 2” or similar “in depth” review by another antitrust or other governmental or regulatory body in relation to the obtaining of a material official authorisation or regulatory clearance (a “Phase 2 Reference”).

3.10 In considering whether the material significance requirement has been satisfied in relation to a Phase 2 Reference Condition, the Executive will take into account the following factors (in addition to those in paragraph 3.5):

- (a) the potential impact of the reference or process on the business of the offeror and/or the offeree company, including the management time, costs and other burdens involved in pursuing it; and
- (b) the utility of requiring the offeror and/or the offeree company to pursue the reference or process where the likelihood of the clearance being obtained is low (because of the low probability either of obtaining clearance at all or of obtaining clearance before the long-stop date).

3.11 The ability of the offeror to demonstrate that the making of a Phase 2 Reference satisfies the material significance requirement, and therefore the willingness of the Executive to consent to the invocation of a Phase 2 Reference Condition, will not be adversely affected by the fact(s) that:

- (a) the offer is also subject to a specific condition in relation to clearance being obtained at the conclusion of the Phase 2 Reference (a “Phase 2 Clearance”) and/or a general regulatory (or “sweeper”) condition (together, a “Phase 2 Clearance Condition”); and/or
- (b) the long-stop date may accommodate the time needed to undertake a Phase 2 Reference.

3.12 Conversely, if an offer is not subject to a Phase 2 Clearance Condition, that will not be considered to support an argument that the making of a Phase 2 Reference satisfies the material significance requirement, such

that the offeror should be permitted to invoke a Phase 2 Reference Condition.

- 3.13 If a Phase 2 Reference is made (and any Phase 2 Reference Condition is waived) but the offer is not subject to a (specific or general sweeper) Phase 2 Clearance Condition, the consequence will be that the offeror will not be able to lapse the offer if the Phase 2 Clearance is not obtained (unless another condition can be invoked). The Executive therefore considers that, from the perspective of the Code, it would be prudent for an offer normally to be made subject to a Phase 2 Clearance Condition and that an offeror should give careful consideration to the consequences of not making the offer subject to such a condition.

(iv) Regulatory clearance conditions

- 3.14 In considering whether the material significance requirement has been satisfied in relation to a specific condition relating to the obtaining of an official authorisation or regulatory clearance or a general sweeper condition (whether following a Phase 2 Reference or otherwise), the Executive will take into account the following factors (in addition to those in paragraph 3.5):

- (a) the significance of the authorisation or clearance to the offeror;
- (b) what action, if any, the offeror would need to take in order to obtain the authorisation or clearance and, if known, the strategic consequences for the offeror if it were to take that action; and
- (c) the consequences for the offeror and its directors if it were to complete the offer without obtaining the authorisation or clearance.

4. Timetable suspensions

- 4.1 If a condition relating to an official authorisation or regulatory clearance has not been satisfied or waived by 5.00 pm on the second day prior to Day 39 of a contractual offer, the Executive will normally suspend the offer timetable either:

- (a) at the joint request of the offeror and the offeree company (Rule 31.4(a)(i)); or
- (b) at the request of either the offeror or the offeree company, provided that the condition relates to a material official authorisation or regulatory clearance, i.e. if the Executive is satisfied that the failure to obtain the authorisation or clearance could (potentially) satisfy the material significance requirement (Rule 31.4(a)(ii)).

4.2 As explained in the Note on the definition of “material official authorisation or regulatory clearance”, the fact that the Executive determines that a condition relates to a material official authorisation or regulatory clearance, and therefore agrees to suspend the offer timetable under Rule 31.4(a)(ii), should not be taken as an indication that the Executive would agree that the failure to obtain the authorisation or clearance would satisfy the material significance requirement so as to permit the offeror to invoke the condition and cause the offer to lapse under Rule 13.5(a). This is because, for an authorisation or clearance to be regarded as a material official authorisation or regulatory clearance for the purpose of suspending the offer timetable, it is only necessary to demonstrate that the failure to obtain the authorisation or clearance could give rise to circumstances in which the material significance requirement would be satisfied.

5. Long-stop dates

(a) Contractual offers

5.1 Under Rule 12.1(a), a contractual offer must include a term that the offer will lapse if, by the long-stop date:

- (a) the acceptance condition has not been satisfied (Rule 12.1(a)(i)); or
- (b) a condition relating to an official authorisation or regulatory clearance has not been satisfied or waived and the Panel consents to the offer lapsing (Rule 12.1(a)(ii)).

5.2 Under Rule 12.2, the Panel will normally consent to an offer lapsing under Rule 12.1(a)(ii) if the condition which has not been satisfied or waived relates to a material official authorisation or regulatory clearance and the action that needs to be taken to obtain the authorisation or clearance either:

- (a) is not sufficiently clear; or
- (b) is sufficiently clear but would give rise to circumstances which satisfy the material significance requirement.

5.3 The Executive therefore expects that if, on the long-stop date, the acceptance condition to the offer has been satisfied but a review by a regulatory body in relation to a material official authorisation or regulatory clearance has not concluded, the offeror will normally be able to lapse its offer. This is on the basis that the action (if any) that needs to be taken to obtain the authorisation or clearance will not normally be sufficiently clear. However, in order for the offer to lapse in these circumstances, the

relevant authorisation or clearance will need to be the subject of a (specific or general sweeper) Category 5 condition.

- 5.4 Under Rule 12.3, except with the consent of the Panel, the long-stop date may only be extended by the offeror with the agreement of the offeree company. To permit an offeror to extend the long-stop date unilaterally would give rise to concerns under General Principle 6 that the offeree company would be hindered in the conduct of its affairs for an unreasonably prolonged period. The Executive will therefore consent to a request from an offeror to extend the long-stop date only in limited circumstances, such as to allow an offeror to align its long-stop date with that of a competing offeror.

(b) Schemes of arrangement

- 5.5 Under Section 3(g) of Appendix 7, where an offer is being effected by means of a scheme of arrangement, the offeror must:

- (a) prior to the court sanction hearing, confirm to the offeree company and the Panel that all of the conditions to the offer have been either satisfied or waived; and
- (b) at the court sanction hearing, undertake to the court to be bound by the terms of the scheme.

- 5.6 The above requirements will not apply if a condition relating to a material official authorisation or regulatory clearance is outstanding, provided that the action that needs to be taken to obtain the authorisation or clearance either:

- (a) is not sufficiently clear; or
- (b) is sufficiently clear but would give rise to circumstances which satisfy the material significance requirement.

- 5.7 The Executive therefore expects that if, prior to the court sanction hearing, a review by a regulatory body in relation to a material official authorisation or regulatory clearance has not concluded, the offeror will normally not be required to take the necessary procedural steps so as to be bound by the terms of the scheme and that the scheme will lapse on its long-stop date. This is on the basis that the action (if any) that needs to be taken to obtain the authorisation or clearance will not normally be sufficiently clear. However, in order for the scheme to lapse in these circumstances, the relevant authorisation or clearance will need to be the subject of a (specific or general sweeper) Category 5 condition.

6. Pre-conditions

This Practice Statement applies in the same way to the invocation of pre-conditions permitted under Rule 13.3.

7. Agreements relating to the invocation of conditions to an offer

This Practice Statement should be read in conjunction with section 3 of Practice Statement 29, which provides guidance in relation to, among other things, the application of Rule 21.2 to agreements relating to the invocation of conditions to an offer.

Practice Statements are issued by the Panel Executive to provide informal guidance to companies involved in takeovers and practitioners as to how the Executive normally interprets and applies relevant provisions of the Takeover Code in certain circumstances. Practice Statements do not form part of the Code. Accordingly, they are not binding on the Executive or the Panel and are not a substitute for consulting the Executive to establish how the Code applies in a particular case.

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