SQUIRE PATTON BOGGS

CAPITAL MARKETS PRACTICE: NEWS ROUND-UP ISSUE NO. 1/2015

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Introduction

Welcome to the latest in our series of regular alerts containing a round-up of news from our capital markets practice. We advise companies, financial advisers and underwriters on all aspects of capital markets and public M&A transactions in all the principal markets of the UK, US, Continental Europe and Asia Pacific. We would be delighted to discuss with you any issues arising out of the items covered in this update.

Takeovers by Scheme of Arrangement: Proposed Changes to Legislation

The Government has published The Companies Act 2006 (Amendment of Part 17) Regulations 2015 (SI/2015 Draft) which will prohibit a company from reducing its share capital as part of a scheme of arrangement where the purpose is to implement certain takeovers or mergers.

In the context of takeovers, there are two main types of schemes of arrangement: a 'transfer' scheme which sees the transfer of shares in the target company to new owners; and a 'cancellation' (also referred to as a 'capital reduction') scheme which is effected through a reduction of the target company's share capital and the issue of new shares to the new owners. Implementation of a 'transfer' scheme requires payment of stamp tax on shares at 0.5% of the consideration paid for the shares, but no such liability flows from the implementation of a 'cancellation' scheme as taxation of the issue of new shares is prohibited by the EU Capital Duties Directive (2008/7/EC).

The Government wishes to put legislation in place as soon as possible so as to limit the scope for companies to bring forward takeovers in order to circumvent the legislation. 'Cancellation' schemes will, however, still be permitted for other purposes such as debt restructuring and intragroup reorganisations.

A copy of the draft SI is available on the UK Government website.

Many larger UK takeover bids for Main Market listed target companies have for many years been effected by way of 'cancellation' schemes. The market will be watching closely to see whether schemes (albeit, in the future, 'transfer' schemes) remain a popular structure for effecting a takeover bid.

Share Dealings by Persons Discharging Managerial Responsibilities: Lessons to be Learnt

The FCA has published a final notice on Reckitt Benckiser Group Plc for inadequate systems and controls to monitor share dealing by two of its senior executives in its own shares. The decision is significant in that the FCA has stated that it expects all listed companies to learn the lessons from this case and to ensure they have the right controls and training in place.

A copy of the Final Notice is available on the FCA website and further details are provided in our stand-alone update available on our website.

B Share Schemes: Proposed Tax Changes

The value to shareholders of cash paid out by companies depends on the tax treatment of the payment. This will vary between shareholders and is heavily influenced by the way the cash is distributed so that the method of distribution can have a major impact on the perceived value to investors. Unfortunately, the complexity of the UK tax system makes it impossible to point to one route that offers the best outcome for all types of shareholder. There is a general perception that income is "bad" and capital is "good" but this is a gross over simplification. To allow shareholders to make their own decision, B share schemes have been used to give shareholders the choice between income and capital tax treatment. A number of structures have developed over the years but, typically, the company makes a bonus issue of new B shares which then either pay a one off cash dividend or can be disposed of for a capital payment.

Advisers have generally sounded a note of caution that HMRC may not play ball and could try to tax the cash as income under existing anti-avoidance rules, regardless of how it is paid out. However, these structures have been quite widely used without apparent objection from HMRC. In December, the Government finally called time on B share schemes and announced in the Autumn Statement that it would change the law to tax all returns to shareholders through B share schemes as income. Draft legislation was published before Christmas and we can expect it to be included in the Finance Bill that will be issued after the Budget on 18 March. Assuming there is no objection from the Labour opposition, there is every chance that the changes will become law by the end of March (when Parliament is dissolved for the May general election).

The new rules are intended to be effective from 6 April 2015 so there remains a short window during which B share schemes can be used to offer shareholders a choice of tax treatment. From April, there may still be occasions when these structures make sense from a company law perspective but it is likely that this route for returning cash to shareholders will largely cease to be relevant.

How Squire Patton Boggs Can Help

We would be pleased to discuss with you in more detail any of the matters raised in this update.

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