

The Panel on Takeovers & Mergers (the “Takeover Panel”) has announced the introduction of new rules in relation to defined benefit pension plans operated by target companies. Bidders, targets and pension plan trustees will need to be prepared for the changes, which will apply from 20 May 2013 onwards.

What Are the Changes?

- The new rules apply in respect of occupational pension plans (either UK or non UK) which: (a) are funded plans sponsored by the target or any of its subsidiaries (including subsidiaries which are not wholly-owned); (b) provide pension benefits, some or all of which are on a defined benefit basis (i.e. the rules do not apply to defined contribution only plans); and (c) have trustees (or in the case of a non UK plan, managers). The rules do not make an exception for pension plans which are immaterial in the context of the target group.
- A bidding company must state, in its offer document, its intentions with regard to employer contributions into the target’s pension plans (including as to funding any plan deficit), the accrual of benefits for existing plan members and the admission of new members. The bidder does not need to comment more widely on the likely repercussions of the offer, and the bidder’s strategic plans for the target, on those pension plans (including as to the strength of the on-going financial covenant provided to the plans).
- If no changes with respect to those matters are intended in relation to the target’s pension plans, a negative statement to such effect must be made.
- The Takeover Panel will hold those making statements of intention during the course of an offer (e.g. the bidder) to such statements for a period of 12 months following the end of an offer period, unless such statements are expressly limited to some other time period or a material change of circumstances has occurred.
- Certain information must be made available to the target pension plan trustees in takeover bids.
- The trustees may (but are not required to) provide, publicly, their own opinion as to the likely effects of the offer and/or the bidder’s strategic plans for the target on the target’s pension plans – this opinion may comment on the impact of the offer (including, for example, its financing) on the likely strength of the on-going financial covenant provided to the pension plans.

- The target board’s circular (in recommended offers, in the offer document) is not required to include the target board’s opinion of the effect of the offer on the pension plans, although the target board may include such an opinion, if it wishes to do so.
- If the bidder and target pension plan trustees reach an agreement on the future funding of the relevant pension plans, a summary of such agreement must be included in the bidder’s offer announcement and offer document and, if the agreement is considered material, the agreement itself must be published on a website by the bidder.

These provisions sit alongside provisions already included in the Takeover Code at the conclusion of a major review in September 2011, requiring a comparable disclosure of information in relation to the likely effects of a bid and a bidder’s strategic plans on target group employee arrangements.

Are These Significant Changes in Practice?

They are unlikely to be. The changes require the public disclosure of certain intentions of the bidder relating to the benefits payable under the target pension plans (with the ability of pension plan trustees and the target board to respond) but will not, in all likelihood, lead to pension plan trustees (or, indeed, target directors) having a stronger position in negotiating the details of a transaction, or preventing a transaction going ahead. The Takeover Panel has made quite clear in its consultation process that it will not play a role similar to that of the Pensions Regulator and that completion of a takeover will not be made conditional on the bidder reaching a suitable funding agreement with target pension plan trustees, whether with or without the involvement of the Pensions Regulator.

In reality, in the case of many recommended takeover offers, where the target company’s group operates a defined benefit pension plan which is in deficit, bidders have, for several years, often been diligent in liaising with target directors and target pension plan trustees upfront, in relation to on-going funding arrangements following an offer. Indeed, in several high profile cases, where agreement on such funding arrangements could not be reached before announcing bids, this had been enough to dissuade certain bidders from proceeding with a transaction. In such cases, significant information might well have been traded upfront between a bidder and pension plan trustees.

The Pensions Regulator can be expected, as has been the case in the past, to continue to be involved in funding disputes, where its involvement is required by the bidder, target or trustees, but the Takeover Code will not require such involvement in bids as a matter of course.

The regulatory changes might at least mean, however, that the bidder cannot completely keep target pension plan issues off the agenda for discussion.

How Helpful Will the Additional Information be that is Disclosed?

Potentially not very helpful, but this will depend on how bidders behave in practice in complying with the new provisions. If bidders merely comply with the letter of these provisions (and offer no further co-operation voluntarily), the results will not necessarily be of significant benefit for targets, pension plan trustees or plan beneficiaries. Whilst this has partly been the experience in relation to the employee disclosure obligations noted above (where bidders have too often simply expressed in offer documentation a general intention to conduct a review on the impact of the takeover on employees after the event), it is hoped that a more open dialogue between bidders and pension plan trustees (with information flow occurring both ways) will continue and more meaningful statements will be included in offer documentation. This might be more likely where pension funding issues are particularly complicated and potentially more serious. The Takeover Code will include more generous exemptions from the usual restrictions applying to conversations with third parties regarding takeover offers, by expressly permitting confidential discussions between the bidder or target and pension plan trustees.

Notably, however, there is no requirement, within the new provisions, for the bidder to actively or constructively engage with target pension plan trustees, either before, during or after a takeover offer.

In relation to the information disclosure provisions to be incorporated in the Takeover Code, those provisions could be described as minimum public information disclosure requirements and may not, without further (voluntary) co-operation from the bidder, allow target pension plan trustees to form their own meaningful views as to the likely impact of the bid on any financial covenant going forward (particularly in the longer term). In the absence of such co-operation, trustees would have to rely on publicly available information which may not give them sufficient insight as to the bidder's current financial position or as to the details of its future plans. The Takeover Code will, however, at least require that the target and, in relation to certain documentation, the bidder, makes available to trustees a copy of the key announcements and documentation in relation to an offer (which would include details, albeit in summary, in relation to the financing of the bidder's offer and the refinancing of any existing debt or working capital facilities of the target).

As regards the format and breadth of public information disclosures expected in future takeover bids, this may well depend, to a great extent, on the nature of the target pension plans concerned on a case by case basis, but will also depend on how specific and/or helpful the bidder is prepared to be in the statements of intention it makes and the extent to which a target board is prepared to recommend a bid where it has less than absolute clarity on such matters.

In the case of hostile bids, one can assume that such statements may not be particularly instructive or helpful although that may not be particularly surprising if, in addition, active engagement with pension plan trustees is difficult. It would also not be unlikely to find that, during hostile bids, the target board and target pension plan trustees would use statements made by hostile bidders in relation to the target's pension plans (or the absence of meaningful statements) as reasons for not recommending a bid or for target shareholders not to accept a bid.

It would also not be surprising if bidders very regularly limited their statements to the standard 12-month period, a period which, obviously, in the life of a pension plan, is extremely short.

If Target Pension Plan Trustees Wish to Express Their Opinions on a Takeover Bid, How are These to be Expressed?

The new provisions oblige the target board to append to its circular (which sets out its views on the offer – in the case of a recommended takeover bid, this will be the offer document itself), an opinion received from the target's pension plan trustees, provided such opinion is received in good time before the circular is published. In other cases, the target is required to publish on a website, operated by or on behalf of it, the trustees' opinion, if received up until 14 days after an offer has become wholly unconditional, and announce such publication. It might be, if the analysis of the impact of a takeover bid on the pension plans is a complex one, that any such opinion can therefore be provided significantly after an offer document has been posted to shareholders. The target board is required to remind trustees of their right to publish such an opinion. Trustees also have the right to publish further opinions if an offer is revised.

Such provisions do not prevent trustees from making their opinions and concerns made known in other ways, as they have done in previous takeover bids where pensions issues have come to the fore. In theory, trustees may, subject always to complying with the Takeover Code, make statements to the media (and other news information services) in relation to their concerns, may (subject to having the legal right to do so) attend and speak at shareholder meetings of the target company to consider a takeover bid (for example, where a takeover is conducted by way of scheme of arrangement) or may attend court hearings convened to approve a takeover and raise concerns at such hearings (as a significant creditor of the company, again, where a takeover is conducted by scheme of arrangement).

The target is required by the Takeover Code to pay for the costs of publishing the trustees' opinion but there is no provision in the Takeover Code requiring that the target pay for the costs of its preparation (including, for example, the costs of any actuarial analysis). However, we expect that in the normal course, under the plan rules themselves, the target would ultimately cover these trustee costs.

What Will Happen if a Bidder Subsequently Takes Action Which is Detrimental to the Target's Pension Plans?

The Takeover Panel will hold bidders to statements of intention they make during an offer for 12 months (or such other period to which their statements are expressly time limited) following the end of an offer period. If a bidder takes actions within such period, contrary to its previously stated intentions (and which were not previously disclosed during the offer), and these are discovered by the target pension scheme trustees or other interested parties, the Takeover Panel might decide to take disciplinary action against the bidder and

its directors for a breach of the Takeover Code. Statements by bidders in offer documentation in relation to pensions will not, however, of themselves, be able to form the basis of an actionable claim brought directly by the trustees.

The Takeover Panel may, however, decide not to take any disciplinary action if a “material change of circumstances” has occurred in the relevant period. It is not clear, at this point, what sorts of developments the Takeover Panel may be prepared to accept as material. Since any such disciplinary action would not, in all likelihood, redress the potential detriment done to a target’s pension plan or its underlying beneficiaries, the Takeover Panel’s sanction powers may well be more useful to trustees in their threatened (rather than in their actual) use.

Because of that threat, it would seem quite likely that bidders will refrain, wherever possible, from taking potentially controversial actions which could impact on the funding of the target’s pension plans until after the 12 month period has expired. If actions can be delayed until such point, it may also allow bidders to escape the potentially politically sensitive disclosures that might otherwise be required (and associated negative PR), whilst the target company is in the public glare. Where actions are taken after such period, such matters would (depending on the nature of the event concerned) potentially fall within the Pensions Regulator’s domain but, at any rate, will not fall within the Takeover Panel’s.

If a bidder is prepared to enter into a funding agreement with the pension plan trustees before or during a takeover bid, it will be this document, rather than the Takeover Code itself, that might prove the best avenue for trustees to deal with their concerns about any subsequent actions by the bidder.

What Happens if the Trustees Enter into a Funding Agreement with the Bidder?

If the bidder enters into such an agreement, a summary should be included in the bidder’s firm offer announcement and in its offer document. If that agreement is also considered “material” (there has long been some debate as to what that concept means) a copy of that agreement must go on public display (i.e. on the bidder’s website). Parties to such agreements should therefore note that the contents of those agreements may not be capable of being kept confidential at the time of the bid.

There is an exemption from the usual prohibition in the Takeover Code, in relation to “offer-related arrangements”, allowing such funding agreements to be entered into by the bidder with pension plan trustees. However, the Takeover Panel has made clear that they would expect such agreements only to relate to future funding of the pension plans and that such agreements must not, for example, impose any obligations or restrictions on the trustees as regards other bidders or potential bidders.

How Can We Help?

Squire Sanders has a wealth of experience in advising both on UK takeover bids and on target company pension plans, whether acting for bidders, targets, or pension trustees. Our M&A and pension teams have seconded members of their staff to both the Panel on Takeovers & Mergers and the Pensions Regulator and sit on working parties who consult on intended rule changes in the areas of UK takeovers and pensions. Consequently, we also understand policies and practices that may not be reflected in any formal and publicly available regulation or guidance in those areas.

If you are involved with a takeover that raises pension issues, please contact any of those individuals whose details are listed below or your usual Squire Sanders contact.

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