Market Abuse Regulation (EU MAR) Q&A

Prepared by the City of London Law Society and Law Society Company Law Committees' Joint Working Parties on Market Abuse, Share Plans and Takeovers Code

*This Q&A on the Market Abuse Regulation (MAR) (the "**Q&A**") has been drafted by the above Joint Working Parties as a suggested approach to implementing certain aspects of MAR, but has not been endorsed by the Financial Conduct Authority. It is subject to review and amendment in the light of practice on the interpretation of the MAR and to any relevant future UK or EU guidance published in relation to MAR.*

It is not intended to be and should not be relied upon as being legal or regulatory advice. Users of this Q&A are encouraged to consult their own advisers directly before taking any action based on the Q&A. None of the members of the Joint Working Parties or their respective firms represents or warrants that it is accurate, suitable or complete and none shall have any liability arising from, or relating to, the use of this Q&A.

Market soundings (Article 11)

Q1. If the bidder and target negotiate the terms of an irrevocable undertaking to accept the offer/vote in favour of the scheme (as applicable) that is intended to be given by target directors, will those communications fall within the market soundings regime?

A1. No.

Rationale: The negotiation of the terms of the irrevocable undertaking involves communications between the bidder and target (represented by its directors) and not communications with a "person entitled to securities" of the target as referred to in Article 11(2). A bidder seeking a recommendation from a target board will approach the target board and put forward an indicative offer that is subject to a number of conditions. These will invariably include a requirement that those target directors who hold shares will give irrevocable undertakings to accept the offer/vote in favour of the scheme (as applicable). If a recommendation is forthcoming, the target directors will agree to provide such undertakings. The approach to the target board is not made in order to ascertain the willingness of the directors to accept the offer/vote in favour of the scheme but in order to obtain a recommendation of the offer (and in considering whether to do so the directors are expected to consider the interests of the company and all its shareholders and not their own personal position). The fact that a decision to recommend will lead to an expectation that the directors will enter into irrevocable undertakings is a consequence and not an objective of the approach, which is not therefore a market sounding. If target board decides to recommend the offer, the terms of the irrevocable undertaking would then typically be negotiated and agreed as between the bidder and target and their respective legal advisers (see Q2 below), and, as noted, all the target directors would then be expected to enter into the agreed form of undertaking.

Q2. Where the terms of an irrevocable undertaking to accept the offer/vote in favour of the scheme (as applicable) intended to be given by target directors have been agreed between the bidder and target as outlined above, will the provision of the agreed form irrevocable to the target directors fall within the market soundings regime?

A2. No.

Rationale: This is merely an ancillary process relating to communications that have already taken place with the target directors (in their capacity as such) in connection with the proposed offer, including the negotiation of a form of irrevocable undertaking as between the bidder and target (as discussed above). In

this context, the process (whether conducted directly by the bidder or by the target company) of providing the final form of irrevocable undertaking to the target directors and gathering executed copies of the same does not involve the communication of inside information "necessary to enable the…[target directors]…to form an opinion on their willingness to offer their securities" as referred to in Article 11(2).

Q3. Will communications between the bidder and shareholders with a view to seeking irrevocable undertakings to accept the offer/vote in favour of the scheme (as applicable) from them fall within the market soundings regime?

A3. Yes, if the shareholders are not target directors (who are covered in Q1 and Q2 above).

Rationale: These would fall within Article 11(2) as they would involve wall-crossing such shareholders and, as referred to in Article 11(2), communicating inside information to them which is "necessary to enable the…[shareholders]…to form an opinion on their willingness to offer their securities".

Q4. In Article 11(2), is a communication within the market soundings regime only if it is made by the bidder – i.e. given the lack of equivalent to Article 11(1)(d)?

A4. No. References to the bidder in Article 11(2) should be read as including references to persons clearly acting as the bidder's agent/on its behalf (e.g. its financial adviser or broker).

Rationale: To read the provisions of Article 11(2) more restrictively would produce an anomalous result.

Q5. Can market soundings be conducted other than in strict compliance with Article 11 and the Implementing Technical Standards?

A5. Yes, non-compliance with the market sounding requirements (when a communication is within Article 11(1) or (2) and inside information is disclosed) does not automatically mean that the communication is unlawful or that the person making the communication is subject to sanctions simply on the basis of non-compliance. This is subject to the obligation under Article 11(3) which must be complied with in all cases (i.e. that the disclosing market participant must consider in advance whether the sounding will involve disclosure of inside information and make a written record of its conclusions and the reasons therefor).

Rationale:

Recital (35) provides that "There should be no presumption that market participants who do not comply with this Regulation when conducting a market sounding have unlawfully disclosed inside information but they should not be able to take advantage of the exemption given to those who have complied with such provisions. The question whether they have infringed the prohibition against the unlawful disclosure of inside information should be analysed in light of all the relevant provisions of this Regulation…".

Article 11(4) states that "For the purposes of Article 10(1) [(unlawful disclosure)], disclosure of inside information made in the course of a market sounding shall be deemed to be made in the normal exercise of a person's employment, profession or duties where the disclosing market participant complies with paragraphs 3 and 5 of this Article" – i.e. compliance with the provisions of Article 11 is mandatory to fall within the safe harbour, but non-compliance does not automatically mean that there has been a breach of Article 10.

The fact that Article 30 (administrative sanctions) does not include reference to breach of Article 11 also lends weight to this analysis.

Article 11(3) imposes a stand-alone obligation that is not specifically limited to the safe harbour set out in Article 11(4).

Stake-building on a takeover

Q6. Will due diligence information that amounts to inside information preclude stake-building pre-announcement as a result of Article 9(4)?

A6. Article 9(4) is expressed not to apply in relation to stake-building. Therefore bidders cannot rely on Article 9(4) to stake-build pre announcement when in possession of any inside information (other than knowledge of their own intention to bid/stake-build – see Q7. above). Bidders will need to consider/apply their judgment on a case by case basis as to whether stake-building is otherwise permitted. For stake-building post-announcement, see Q9.

Q7. Will due diligence information that amounts to inside information cease to be inside information once a bid is announced if the bid price is in excess of the price effect the inside information had been expected to have (i.e. if the impact of any inside information would be absorbed by the bid premium)?

A7. It will be necessary to consider this issue/apply judgment on a case-by-case basis to determine whether in a particular instance the information has ceased to be inside information. Where a recommended bid has been announced it may well be possible for the bidder to come to the view that the information is no longer inside information including on the basis that its impact will have been absorbed by the recommended price.

Where a non-recommended or hostile bidder has inside information about the target, it may also be possible for the bidder to come to the view that the bid price it has announced effectively absorbs the impact of that inside information, but it may be harder to reach this conclusion than on a recommended deal. However, once the defence document has been published by the target board it would normally be the case that the information is no longer inside information. Shareholders are required to be given sufficient information and advice to enable them to reach a properly informed decision on an offer; no relevant information should be withheld from them.

PDMR dealings (Article 19)

Q8. Where a PDMR has entered into an irrevocable undertaking outside a closed period, can they satisfy that irrevocable undertaking during a closed period?

A8. Yes.

Rationale: The point at which the PDMR conducts the transaction is the point at which they enter into the irrevocable undertaking rather than the point at which they satisfy it. Provided it is entered into outside a closed period it can therefore be satisfied during a closed period (see Q3 and Q4 in Part 1 of these Q&As).

It should also be noted that, where a bid is announced at the same time as interims/prelims are released, irrevocables that have been signed and held in escrow for release at the time of the bid being announced will not be treated as being dealings during the immediately preceding closed period as they only become effective upon release from escrow (at which point the closed period has ended).

Q9. During a closed period under Article 19(11) can a PDMR vote in favour of/enter into an irrevocable undertaking to vote in favour of a takeover conducted by way of scheme of arrangement?

A9. Yes. Note, however, that where an irrevocable undertaking on a scheme includes an obligation to accept a contractual offer if the transaction structure is switched by the bidder, entering into the irrevocable undertaking should be treated in the same way as entering into an irrevocable undertaking in respect of a contractual offer (see Q 12. below).

Rationale: This does not involve the PDMR conducting a transaction within Article 19, but rather involves them voting/giving an undertaking to vote their shares in favour of the scheme of arrangement. In addition, the transfer of shares on completion of a scheme of arrangement by order of Court would not be restricted

during a closed period as it would take place automatically by operation of law rather than being a trading by the PDMR (see Recital (61) to MAR).

Q10. During a closed period under Article 19(11) can a PDMR accept/enter into an irrevocable undertaking to accept a contractual takeover?

A10. Unless an exemption applies, no.

Rationale: This involves the PDMR conducting a transaction within Article 19 (subject to Q10. above (i) where an acceptance is made during a closed period pursuant to an irrevocable undertaking which was entered into prior to commencement of the closed period or (ii) where an irrevocable is released from escrow at the point of announcement in the case of a bid which is announced at the same time as interims/prelims are released).

Q11. Do any of the matters referred to in Q9 or Q10, whether they occur within (if permitted) or outside a closed period, need to be disclosed in accordance with Article 19(1)?

A11.1 Voting in favour of/entering into an irrevocable undertaking to vote in favour of a scheme does not need to be notified under Article 19(1).

Rationale: This does not involve a transaction being conducted on the account of the PDMR. In addition, no notification would be required in relation to the transfer of shares on completion of a scheme of arrangement by order of Court as the target company would be delisted upon the scheme becoming effective.

A11.2 Entering into an irrevocable undertaking to accept a contractual offer does not need to be notified under Article 19(1). Accepting a contractual offer (whether pursuant to an irrevocable undertaking or otherwise) does not need to be notified until the offer becomes wholly unconditional.

Rationale: Pursuant to Article 10(2)(i) of Regulation (EU) 2016/522 conditional transactions need only be notified on occurrence of the conditions and actual execution of the transaction. Even when the irrevocable undertaking is satisfied by submission of an acceptance of the offer, that acceptance remains conditional until the offer becomes unconditional. Notification would not therefore be required under Article 19(1) until the offer became wholly unconditional. Acceptances made by PDMRs prior to the offer becoming wholly unconditional should be notified by them when the offer becomes wholly unconditional, and acceptances by PDMRs made after the offer has become wholly unconditional should be notified when made.

Note that, notwithstanding this analysis in respect of MAR, disclosure of irrevocable undertakings and acceptance/approval levels would need to be announced in accordance with any applicable takeover legislation/regulation.

15 August 2016

APPENDIX

Members of the City of London Law Society and Law Society Company Law Committees' Joint Working Parties on Market Abuse, Share Plans and Takeovers Code

Victoria Younghusband	Charles Russell Speechlys
Stephanie Maguire	Freshfields Bruckhaus Deringer
Vanessa Knapp	
Carol Shutkever	Herbert Smith Freehills
Caroline Chambers	Ashurst
William Underhill	Slaughter and May
Lucy Fergusson	Linklaters
Jaya Gupta	Allen & Overy
Kathryn Roberts	Clifford Chance
S Sagayam	Gibson Dunn & Crutcher
David Pudge	Clifford Chance
James Roe	Allen & Overy
Sarah Hawes	Herbert Smith Freehills
Simon Jay	Cleary Gottlieb Steen & Hamilton
Nicholas Holmes	Ashurst
Michael Hatchard	Skadden, Arps, Slate, Meagher & Flom
Robert Adam	Baker & McKenzie
Elizabeth Wall	Allen & Overy
J Wall	Wedlake Bell
Stephen Hewes	Freshfields Bruckhaus Deringer
Chris Randall	Norton Rose Fulbright
Sharon Jenman	Ashurst
Richard Spedding	Travers Smith
Chris Pearson	Norton Rose Fulbright
Kathy MacDonald	Norton Rose Fulbright
Richard Ufland	Hogan Lovells
C Haynes	Gibson Dunn & Crutcher
Mark Bardell	Herbert Smith Freehills
Paul Ellerman	Herbert Smith Freehills
Paul Randall	Ashurst
Tamsin Nicholds	Hogan Lovells
Richard Hough	Allen & Overy