

Chapter 11

Tender offers

Introduction

In a tender offer, the bidder goes directly to the shareholders of the target company with an offer to buy their shares. Each shareholder individually decides whether or not to tender with (friendly) or without (hostile) the cooperation of the target's board of directors. In contrast, a merger is a collective voting decision where the acquiror acquires the entire company if the target's shareholders approve the merger. In a merger, the acquiror generally needs the approval of the target's board of directors to present the transaction for a shareholder vote, which is not the case in a tender offer. There are two types of tender offers, cash tender offers (ie, tender offers for cash) and exchange offers (ie, tender offers for securities).

Exchange Act regulation of tender offers

Reporting requirements

Section 13(d) of the Exchange Act requires anyone who acquires 5% or more of an equity security registered under Section 12 of the Exchange Act to report the acquisition and his intentions for the issuer of the security. (Schedule 13D is discussed above under the heading 'Ownership reports' in Chapter 9, 'Exchange Act registration and reporting'.)

Disclosure requirements for registered equity securities

Section 14(d) of the Exchange Act is the basic section that regulates tender offers. Under this Section, the bidder must make appropriate disclosure before commencing the tender offer. Additionally, Section 14(d)(4) requires disclosure by anyone making a solicitation or recommendation to the holders of the target's securities to accept or reject a tender offer. Under Sections 14(d)(5), (d)(6) and (d)(7), and related Securities and Exchange Commission (SEC) rules, a tender offer subject to Section 14(d) must comply with certain procedural and substantive regulations described below. Rule 14e-2 requires the target's management to disclose its position on the tender offer, which disclosure in turn triggers the target's obligation to file a Schedule 14D-9.

Antifraud and substantive provisions for all securities

Section 14(e) of the Exchange Act is an antifraud provision that makes it unlawful for any person making a tender offer (or defending against one) to make a false statement of material fact or misleading omission of material fact, or to engage in any fraudulent, deceptive or manipulative act or practice, in connection with any tender offer. Additionally, the SEC has adopted rules under Section 14(e), described below, which provide certain procedural and substantive requirements.

What is a tender offer?

A 'tender offer' is generally thought to be an offer to purchase that is made 'publicly', to all or substantially all of the shareholders of a corporation. However, it is not defined in the Exchange Act. The courts define the term 'tender offer' on a case-by-case basis, and a broad definition is used so as to effectuate the purposes of the Exchange Act and its tender offer provisions (ie, protection of the public and of investors). Consequently, all of the relevant facts must be considered in determining whether a tender offer exists.

Eight-factor test

Most courts refer to the eight-factor test given in *Wellman v. Dickinson*, 475 F. Supp 783 (S.D.N.Y 1979). However, not all eight factors need be present for the court to find a tender offer. The eight factors are listed below.

- a) Was there an active and widespread solicitation of shares by the offeror?
- b) Was the solicitation for a substantial percentage of the outstanding stock?
- c) Was a premium price offered over the market price before the offer?
- d) Were the terms of the offer firm and fixed?
- e) Was the offer contingent on the tender by shareholders of a fixed minimum number of shares?
- f) Was the offer by shareholders open for only a limited time?
- g) Was there pressure put on shareholders to sell?
- h) Were there public announcements accompanying the offer?

Hanson Trust 'totality of the circumstances' test

In the *Hanson Trust* case, 774 F.2d 47 (2d Cir. 1985), the Second Circuit declined to elevate *Wellman* to a 'litmus test', and stated that the question:

whether a solicitation constitutes a 'tender offer' within the meaning of Section 14(d) turns on whether, viewing the transaction in the light of the totality of the circumstances, there appears to be a likelihood that unless the pre-acquisition filing strictures of Section 14(d) are followed there will be a substantial risk that solicitees will lack information needed to make a carefully considered appraisal of the proposal put before them.

Acquisitions over a stock exchange

Normally, acquisitions made over a stock exchange in normal market transactions would not be a tender offer. However, under appropriate circumstances (for example, if the eight-factor test of *Wellman* were met), open-market purchases could amount to a tender offer.

Negotiated purchases

Similarly, although privately negotiated purchases ordinarily do not constitute tender offers, under appropriate circumstances (for example, when enough of the *Wellman* factors are pre-

sent, or when the ‘totality of the circumstances’ so dictates) negotiated purchases may amount to a tender offer.

Alternative test for open-market and negotiated purchases

Still another test, broader than the eight-factor test of *Wellman, supra*, and designed to apply to open-market and negotiated purchases, was applied by the court in *S-G Securities, Inc. v. Fuqua Investment Co*, 466 F. Supp. 1114 (D. Mass. 1978). Under the *S-G Securities* test, a tender offer is present if there is:

- a publicly announced intention by the bidder to acquire a block of the target’s stock, for the purpose of acquiring control of the target; and
- a subsequent rapid acquisition by the bidder of large blocks of stock through open-market and privately negotiated purchases.

Tender offers rules for registered equity securities: Section 14(d)

Application of section 14(d) of the Exchange Act

Section 14(d) of the Exchange Act and its related rules apply to tender offers for any class of equity securities registered under Section 12 of the Exchange Act that, if successful, would result in the bidder beneficially owning more than 5% of the class of securities tendered.

If Section 14(d) applies, Regulation 14D requires the following.

Pre-commencement communications

Communications concerning a contemplated tender offer may be distributed before commencement of a tender offer. However, generally, the communication must be filed with the SEC on the date of first use.

When a tender offer commences

A tender offer commences when the bidder first publishes, sends or gives to security holders of the target the means of tender, ie, the transmittal form or a statement how it may be obtained. This is true even if there is no current offer by the bidder to purchase securities.

Disclosure of information

The bidder must make the following disclosures in connection with the tender offer:

Schedule TO. A bidder must file Schedule TO with the SEC (with copies delivered to the target, competing bidders and all stock exchanges on which a target’s stock is traded) when the tender offer commences.

The disclosures required by Schedule TO include:

- a) a plain English summary term sheet;
- b) target company identifying information;
- c) identity and background of the bidder;
- d) terms of the transaction;

- e) past contacts, transactions or negotiations with the target;
- f) purposes of the transactions;
- g) source and amount of funds;
- h) persons retained, employed, or to be compensated in connection with the offer;
- i) if material to a decision by a potential tendering shareholder, financial statements of the bidder; and
- j) if material to a decision by a potential tendering shareholder, certain additional information about: the relationships between the bidder, the target, and their respective officers and directors; regulatory and antitrust issues affecting the transaction; applicability of the margin regulations (governing the use of securities as collateral for loans); pending litigation affecting the offer; and other information material to the tendering shareholders.

Disclosure and publication of tender offer documents. In addition to filing the Schedule TO, the bidder must (both as a practical and a legal matter) take steps to inform the public of the offer. In addition to satisfying a disclosure requirement, the offer is generally deemed to commence on the date the means to tender are first published, sent or given to shareholders. Typically, this will happen in one of two ways: long-form publication or summary publication.

- *Long-form publication.* Long-form publication essentially requires the bidder to publish the offer (which must include or summarize the Schedule TO) in a newspaper of general circulation. Because this produces a rather lengthy (and expensive) advertisement, it is rarely used.
- *Summary publication.* Summary publication consists of a short advertisement, similar to a ‘tombstone’ advertisement that gives the essential terms of the offer and states where copies of the complete offer materials may be obtained.

Target’s recommendation. Regulation 14D also regulates the disclosure required in the target’s recommendation and its dissemination to shareholders.

Substantive requirements

In addition to requiring disclosure, Section 14(d) also imposes the following substantive requirements on tender offers. They are intended to ensure minimum standards of fairness and to curb abuses.

- a) *Withdrawal right.* The offeree may change his mind and withdraw the securities that he tendered and deposited with the offeror at any time while the offer remains open.
- b) *Prorating in a partial tender offer.* Where the bidder seeks to purchase less than all of the issuer’s outstanding stock and a greater number of shares are offered than the bidder intends to purchase, it must purchase shares *pro rata* from each person who tenders.
- c) *Opening the offer equally to all security holders: the ‘all holders’ requirement.* A tender offer must be open to all holders of the securities for which the offer is made.
- d) *Equal treatment of all security holders in the price paid for their securities: the ‘best price’ requirement.* The consideration paid to any security holder in the offer must be the highest consideration paid to any other holder during the offer.

- e) *Limited subsequent offering period.* After the initial offering period has expired and after the successful completion of a tender offer, a third-party bidder may provide a subsequent offering period during which securityholders can tender their securities into the offer without withdrawal rights. This subsequent offering period may last from three to 20 business days.

Offers requiring registration under the Securities Act

Where a tender offer involves the public offer of the bidder's securities to the target's shareholders, the bidder must also register the subject securities under the Securities Act (unless an exemption applies). In that case, the bidder must file both Schedule TO and the appropriate Securities Act registration form with the SEC, and must distribute both the tender offer documents and the prospectus for the securities offered to the shareholders of the target.

Exemptions to section 14(d) of the Exchange Act

The tender offer rules of Section 14(d) do not apply in the situations described below.

5% limitation

Section 14(d)(1) is not applicable if, after consummation of the offer, the person making the offer is not the owner of at least 5% or more of the class of equity security tendered.

Equity securities

Only equity securities registered under Section 12 of the Exchange Act are covered by Section 14(d)(1), ie, registered common stock, as opposed to debt securities, or bonds.

Offers made by the issuer for its own securities

Offers made by the issuer for its own securities are not covered by Section 14(d) but are covered by the issuer self-tender rules of Section 13e-4 of the Exchange Act.

Tender offer rules for all securities: Section 14(e)

Section 14(e) of the Exchange Act and its related rules apply to tender offers for any security regardless of whether it is an equity security or registered under Section 12 of the Exchange Act. Section 14(e) of the Exchange Act is a broadly-worded, antifraud provision that prohibits any person from making material false statements or misleading omissions, and from engaging in any fraudulent, deceptive or manipulative acts or practices, in connection with a tender offer or a solicitation of securityholders in opposition to or in favor of a tender offer.

If Section 14(e) applies, Regulation 14E requires the following conditions to be met.

Duration

The bidder must keep its offer open for at least 20 business days from the date the tender offer commences. The offer must also remain open for at least 10 business days from the date that notice is first published, sent or given to securityholders of any change in the percentage of the class of securities being sought, in the consideration offered, or in the dealer's soliciting fee. The minimum time period an offer must remain open following material changes in the terms of the offer or in information concerning the offer (other than

a change in the percentage of the class of securities being sought, in the consideration offered or in the dealer's soliciting fee) will depend on the facts and circumstances. These include the relative materiality of the terms of information and the nature of the dissemination required.

Prompt payment or return of tendered securities

The bidder must pay the consideration offered or return the securities deposited by securityholders promptly after the termination of the tender offer, which generally means no later than the third business day after the date of the transaction.

Target company recommendations

Within 10 business days from the date the bidder's tender offer commences, the target company must publish, send or give to securityholders a statement of its position, disclosing whether it:

- a) recommends accepting or rejecting the bidder's tender offer;
- b) expresses no opinion and is remaining neutral; or
- c) is unable to take a position concerning the bidder's tender offer. The statement must also include the reasons for the target's position (including its inability to take a position).

Insider-trading prohibited: disclose or abstain from trading

Any person who possesses material information concerning a tender or proposed tender offer by another person is prohibited from trading in target securities (or any related securities or related options) if:

- the bidder has commenced or taken a substantial step to commence a tender offer; and
- the person who possesses the information knows or has reason to know that the information is non-public and was acquired from the bidder, the target, or any person acting on their behalf, unless the information and its source are publicly disclosed within a reasonable time before the trade.

This prohibition does not apply to (a) purchases by a broker or another agent on behalf of the bidder and (b) sales by any person to the bidder.

No purchases outside the offer

The bidder is prohibited from purchasing any securities of the class tendered and any related securities outside the tender offer. This provision is intended to prevent the bidder from manipulating the market price during the offer or from giving a person selling outside the offer a different deal than that received by persons tendering shares into the offer.

No false announcements

A bidder is prohibited from publicly announcing plans to make a tender offer:

- a) without an intent to commence the offer within a reasonable time and complete the offer;
- b) with the intent to manipulate the price of the bidder's or target's securities; or
- c) without a reasonable belief that the bidder will have the means to purchase the securities sought in the offer.

Cross-border tender offer for a foreign target – Tier I and Tier II

The exemptions for cross-border tender and exchange offers for the securities of foreign private issuers are designated Tier I and Tier II. Neither of the exemptions relieves issuers, third-party bidders or other persons from the antifraud or anti-manipulation rules or the civil liability provisions of the U.S. securities laws.

Tier I

The Tier I exemption provides a complete exemption from U.S. tender offers (both issuer and third-party) and going-private regulation so long as:

- a) U.S. holders own 10% or less of the class of securities sought in the tender offer;
- b) U.S. holders participate in the offer on terms at least as favorable as those offered to any other holders subject to several exceptions, described below;
- c) bidders provide security holders with the tender offer circular or other offering document, in English, on a comparable basis to that provided to other security holders; and
- d) bidders that would otherwise have to file a tender offer statement (Schedule TO) with the SEC must submit (rather than file) an English language translation of the offering materials to the SEC under cover of Form CB and, in the case of a foreign offeror, file a consent to service on Form F-X. Also, the target company may, in lieu of filing its response under Schedule 14-D9, submit its home jurisdiction response materials under cover of Form CB.

The nationality of the bidder does not matter. U.S. bidders may rely on the exemption. The target must be a foreign private issuer and not an investment company (other than a registered closed-end investment company).

The equal-treatment requirement [paragraph b) above] mandates not only equal type and amount of consideration, but also equality in procedural terms of the tender offer (such as duration, pro-rationing and withdrawal rights).

Exceptions to the equal treatment requirement

Cash-only exception. U.S. holders may be offered only cash if the bidder has a reasonable basis to believe that the cash is substantially equivalent to the value of the securities and any cash or other consideration offered to non-U.S. holders. To ensure equivalent value, if the offered security is not a ‘margin security’ under Regulation T, the offeror must provide (upon the request of the SEC or a U.S. security holder) an opinion from an independent expert stating that the cash-only consideration is substantially equivalent to the securities and any cash offered outside the United States. If the offered security is a margin security, no opinion is needed.

Blue sky exception. In an exchange offer, the offeror may also exclude U.S. holders in any state that:

- (i) does not have an applicable blue sky exemption (for an offer exempt from Securities Act registration under Rule 802 discussed below); or
- (ii) does not register or qualify the offer after a good faith effort by the offeror to do so (for an offer registered under the Securities Act).

However, in both cases the offeror must offer those security holders cash consideration instead of excluding them, if it has offered cash consideration to security holders in another state or in a jurisdiction outside the United States.

Tier II

The Tier II exemption provides relief from selected provisions of the tender offer rules for issuer and third-party tender offers when:

- the subject company is a foreign private issuer (and not an investment company, other than a registered closed-end investment company); and
- U.S. security holders own no more than 40% of the class of securities sought in the tender offer.

As with Tier I, the bidder's nationality does not matter. The exemptions address a number of provisions that frequently conflict with home jurisdiction regulations (principally the U.K. Takeover Code), and from which the SEC staff has from time-to-time granted relief on a case-by-case basis. The exemptions include:

- a) equal treatment of target security holders (the 'all holders' and 'best price' requirements);
- b) notice of extensions of the offer;
- c) prompt payment for or return of tendered securities;
- d) subsequent offering period withdrawal rights; and
- e) extension of the offer after reduction or waiver of minimum tender condition.

The Tier II bidder must comply with the remaining tender offer provisions, including the procedural, disclosure and filing requirements. U.S. tender offer documents (for example, Schedule TO), rather than Form CB, must be used in a Tier II tender offer. Additionally, Tier II transactions are not exempt from the 'going private' provisions of Rule 13e-3 under the Exchange Act.

Rule 802

Rule 802 provides an exemption for offerings of securities in exchange for the securities of foreign private issuers in an exchange offer or business combination. The exemptions do not relieve issuers, third-party bidders or other persons from the anti-fraud or anti-manipulation rules or the civil liability provisions of the securities laws.

Rule 802 provides an exemption from Securities Act registration for offers and sales in any exchange offer for a class of securities of a foreign private issuer, or in any exchange of securities for the securities of a foreign private issuer in any business combination, if the U.S. holders of the foreign subject company hold no more than 10% of the securities that are the subject of the exchange offer or business combination.

For the exemption to apply, U.S. holders must participate in the exchange offer or business combination on terms at least as favorable as the other holders of the subject securities (subject to an exception comparable to the Tier I blue sky exception). The exemption is not con-

ditioned on delivery of any specific form of disclosure documents, but any information disseminated to holders of the subject securities or published in the home jurisdiction must be similarly disseminated or published in English for U.S. holders. This information must also be submitted in English on Form CB to the SEC along with, in the case of a foreign offeror, a Form F-X consent to service.

The Rule 802 exemption covers only the issues of the securities and the transactions in which the securities are exchanged. It does not provide an exemption to affiliates or others for resales of the issuer's securities. Securities acquired in a Rule 802 transaction are restricted securities if the securities for which they were exchanged were restricted securities in the hands of the holders. Conversely, the securities are unrestricted (and thus freely tradable), if the securities for which they were exchanged were unrestricted, except by affiliates of the issuer in whose hands they will constitute control stock.

Blue sky compliance

There is no general exemption from state blue sky laws that parallels Rules 800-802. Therefore, issuers must ensure that they consider the effect of blue sky laws before relying on these rules. However, to the extent that the offered securities are listed on a national stock exchange (for example, the New York Stock Exchange) or quoted on the Nasdaq National Market, federal regulation has preempted state registration requirements.

The MJDS and tender offers

Requirements

For tender offers for Canadian targets, the Multijurisdictional Disclosure System (MJDS) provides relief from the U.S. tender offer rules. The target must be a Canadian foreign private issuer, with less than 40% of its stock held in the U.S. The bidder is entitled to rely on a conclusive presumption that the issuer is a foreign private issuer and that U.S. holders hold less than 40% of the subject class of securities unless:

- i) the bidder has actual knowledge to the contrary;
- ii) the issuer's most recent annual report or AIF indicates that U.S. holders hold more than 40%; or
- iii) the aggregate trading volume on Nasdaq and all U.S. exchanges exceeds that of all Canadian exchanges and the CDN over the 12 months preceding the tender offer.

The offer must comply with Canadian tender offer rules, and the issuer must not obtain any regulatory relief from Canadian requirements that provide protections similar to those provided by the U.S. tender offer rules. Bidders of any nationality may rely on MJDS for cash tender offers. However, only Canadian issuers may use MJDS for exchange offers.

Share ownership

Hostile bidders may rely on a presumption that a target satisfies the non-ownership test if:

- the target's U.S. or Canadian public filings do not disclose otherwise; and

- reported trading volume from all U.S. markets does not exceed reported trading volume in all Canadian markets, unless the bidder has actual knowledge to the contrary.

Once an offer is commenced under the MJDS, competing bidders may also use the MJDS. This is so even if the target's U.S. ownership goes over 40%, as sometimes happens when U.S. arbitrageurs become involved, or if the original bid was made under the MJDS in reliance on the presumption based on trading volume and actual U.S. ownership turned out to be greater than 40%.

SEC filing

Tender offer materials are prepared under Canadian requirements and, if the target's securities are registered under the Exchange Act, are filed with the SEC under cover of Schedule 14D-1F. The target company's response is filed under Schedule 14D-9F.

Exchange offers

Where securities are offered, qualifying Canadian bidders may file MJDS Securities Act registration statements on Forms F-8 or F-80 (the MJDS exchange offer forms), or Form F-10 (the general, all-purpose MJDS form). The Registration Statement is effective upon filing and there is no SEC review, other than to check the bidder's eligibility to use the selected form.

Blue sky compliance

Where securities are offered, MJDS transactions must comply with the state blue sky laws. The states have not adopted blanket exemptions for MJDS exchange offers. Where the issuer's securities are listed on a U.S. national stock exchange or the Nasdaq National Market, blanket exemptions are available. However, for other transactions, the securities must be registered or exempt in any state where holders of the target's securities reside. Most states have exemptions for transactions effected by shareholder vote, but not for exchange offers. State exemptions are not uniform, and must be reviewed on a state-by-state basis.

A 50-state blue sky filing can be costly and administratively burdensome. Additionally, the filings are not automatically effective, and the states reserve the right to review them before declaring them effective so the offer can be consummated. Many states have adopted procedures for expedited seven-day review of Form F-8 registration statements. Normally, states have not raised significant comments or caused delays, but the issuer can never be sure in advance that a state will not have significant comments or cause delay through slow processing of the filing. Accordingly, particularly in smaller deals, issuers seek to minimize the number of states in which they must file by seeking out exemptions.

Going private transactions

Unlike the Tier I exemption, the MJDS does not provide an exemption from the 'going private' provisions of Rule 13e-3 under the Exchange Act.

‘Stop at the border’ offerings

Foreign private issuers making share exchange offers have frequently used a technique sometimes referred to as ‘stop at the border’ or ‘vendor placement’ to avoid Securities Act registration. Securities that would otherwise be delivered to U.S. holders are instead delivered to a trustee and sold in the issuer’s home market. The trustee pays the net proceeds of the sale to the U.S. holders.

‘Stop at the border’ transactions still must comply with or obtain exemption from U.S. tender offer rules if the target’s securities are registered under the Exchange Act. For a long time, the SEC staff would issue no action letters for these transactions only if the issuer guaranteed that U.S. holders would receive a specified minimum payment per share. (The no action letters confirmed that Securities Act registration was not required and provided relief from the equal treatment requirements of the tender offer rules applicable to Exchange Act registered securities.) Recently, the staff has granted no action relief without the guaranteed minimum payment.

While deliberating on the scope of the cross-border exemptions to be included in the cross-border rules, the SEC considered and rejected the possibility of granting blanket relief for ‘stop at the border’ transactions in a rule, but stated that no action relief would continue to be available on a case by case basis.

Complying with U.S. domestic tender offer rules

Where neither the MJDS nor the exemption for cross-border tender offers provide relief, tender offers for a class of securities registered under the Exchange Act must comply with the filing, disclosure and procedural requirements of the SEC’s tender offer rules.

Where the bidder will issue securities and neither the MJDS nor any exemption from registration is available, the bidder must register the securities under the Securities Act, normally using Form F-4.

Form F-4 registration statements filed in tender offers and business combinations are subject to SEC review, and the offer or combinations may not be consummated until the SEC’s review and comment process is completed.

In the absence of a listing of the bidder’s shares on a U.S. exchange or the Nasdaq National Market, or some other exemption, registration under state blue sky laws is also required. State regulators may feel freer to comment on Form F-4 filings than on MJDS filing, raising the possibility of a more burdensome and lengthy state review process.

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