

UK Takeovers – New Judiciary Practice Statement for Schemes of Arrangement

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A UK scheme of arrangement is a court-approved mechanism under the UK Companies Act 2006 which permits a company to enter into a compromise or arrangement with its shareholders and/or its creditors or any class of the company, subject to the receipt of requisite shareholder approvals and court sanction. Schemes are flexible corporate tools and have become the preferred corporate structure for implementing takeovers in the UK.

Accordingly, whilst takeovers in the UK are primarily regulated by the UK City Code on Takeovers and Mergers, it is also important to understand the relevant provisions of the 2006 Act, the case law underlying such provisions and the court procedure for a scheme. On 30 June 2020, the Judiciary of England and Wales published [Practice Statement \(Companies: Schemes of Arrangement under Part 26 and Part 26A of the Companies Act 2006\)](#) that provides helpful guidance on this.

The new practice statement sets out the practice to be observed on applications to the courts to convene meeting(s) for shareholders to approve and sanction a scheme, with a view to ensuring issues concerning shareholder class composition, the convening of shareholder meetings and the court's jurisdiction to sanction the scheme are identified and resolved early on in the scheme process.

It replaces Practice Statement (Companies: Schemes of Arrangement) [2002] 1 WLR 1345, issued in 2002 with the aim of avoiding class composition issues arising late in the scheme process depriving the court of jurisdiction to sanction the scheme, and reflects and consolidates certain developments in court practice on schemes since 2002.

Typical steps in the scheme process

There is no 'typical' scheme as the structure ultimately depends on the purpose for which it is used and the company's particular circumstances (including its group structure). For example, a scheme can be used for an intra-group reorganisation (such as inserting a new holding company), a debt restructuring (such as writing off debt and effecting debt for equity swaps) or a takeover, and the structure of the scheme would be different for each of such transactions.

However, in the context of a takeover, a scheme would ordinarily involve the following steps:

- the target applying to the courts under section 896 of the 2006 Act to convene a meeting (or meetings) of the target's shareholders (or classes of such shareholders) to approve the transfer of the entire issued share capital of the target to the bidder;
- a court hearing to approve the convening of such meeting(s) (Convening Hearing);
- the dispatch of a scheme circular to the target's shareholders notifying them of such meeting(s) and providing certain prescribed information;
- shareholder meeting(s) to approve the scheme which would require a majority in number representing 75% in value of the target's shareholders (or each class of the target's shareholders) voting in favour of such scheme;
- the target applying to the courts under section 899 of the 2006 Act to sanction the scheme; and
- a court hearing to sanction the scheme (Sanction Hearing).

Highlighting issues at the Convening Hearing

The new practice statement states that it is the applicant's responsibility to draw to the court's attention at the Convening Hearing, any issue:

- which may arise as to the composition of classes of the target's shareholders or which otherwise affects the conduct of the relevant shareholder meeting(s);
- on whether the court has jurisdiction to sanction the scheme; and
- which might lead the court to refuse to sanction the scheme (other than any issue on the merits or fairness of the scheme which would be addressed at the Sanction Hearing).

The court will then consider whether to determine such issue at the Convening Hearing or whether to give directions for the resolution of that issue.

Notifying affected persons

As a new practice point, the new practice statement states that where an application is made to convene a shareholder meeting (or meetings) in respect of a scheme which gives rise to any of the issues above, the applicant should, prior to the Convening Hearing (unless there are good reasons for not doing so), take all reasonable steps to notify any affected person of the following matters:

- the fact that the scheme is being promoted;
- the purpose which the scheme is designed to achieve and its effect;
- the shareholder meeting(s) which the applicant considers will be required to consider the scheme and the composition of such meeting(s);
- any other matters that are to be addressed at such hearing;
- the date and place fixed for such hearing;
- the fact that such persons are entitled to attend such hearing and the relevant Sanction Hearing; and
- how such persons may make further enquiries about the scheme.

Such notification must be given to such persons in sufficient time to enable them to consider what is proposed, to take appropriate advice and, if so advised, to attend the Convening Hearing. The applicant will be required to provide evidence at the Convening Hearing to explain the steps taken to give the notification and the responses to such notification.

The new practice statement notes that shareholders may still raise objections based on the issues above at the Sanction Hearing; however, the courts will expect them to give good reason why they did not raise them at the Convening Hearing.

Class composition

A scheme can only proceed if a majority representing 75% in value of the target's shareholders or each class of the target's shareholders votes for the scheme. The courts have held that a class must be confined to those persons whose rights are not so dissimilar as to make it impossible for them to consult together with a view to their common interest. If the court order made at the Convening Hearing incorrectly specifies the class meeting(s) that should be convened, there is a risk that shareholders may object to the sanctioning of the scheme on such basis.

The new practice statement reiterates the position in the former practice statement that it is the applicant's responsibility to determine whether more than one meeting of shareholders is required by the scheme and if so, to ensure that such meeting(s) are properly constituted.

In considering whether to order the convening of the relevant scheme shareholder meeting(s), the court will consider whether more than one meeting is required and, if so, the appropriate composition of the meeting(s). Such order may include an order giving affected persons a limited amount of time to apply to the courts to vary or discharge such order.

Judges

The new practice statement states that applications to convene a shareholder meeting (or meetings) to approve the scheme may be listed before either an Insolvency and Companies Court judge or a High Court judge. However, if such application is in respect of a scheme which gives rise to any of the issues above, such application should be listed before a High Court judge.

The new practice statement also states that all applications for the sanction of the scheme should be listed before a High Court judge. In addition, the same High Court judge presiding over the Convening Hearing should, if possible, preside over the Sanction Hearing as well.

Explanatory Statements

Under section 897 of the 2006 Act, the notice summoning the target shareholder meeting(s) must be accompanied with a statement explaining the effect of the scheme and state any material interests of the target's directors and the effect on such interests of the scheme in so far as it is different from the effect on like interests of other persons.

In line with established practice, the new practice statement states that in addition to the requirements set out in section 897 of the 2006 Act, explanatory statements should:

- be in a form and style appropriate to the circumstances of the case, including the nature of the shareholder constituency, and should be as concise as the circumstances admit;
- explain the commercial impact of the scheme;
- provide the target's shareholders with such information as is reasonably necessary to enable them to make an informed decision as to whether the scheme is in their interests; and
- explain how to vote on the scheme.

Where a document is incorporated into the explanatory statement by reference, readers should be directed to the material part(s) of such document.

As a new practice point, the new practice statement goes on to state that the court will consider the adequacy of the explanatory statement at the Convening Hearing. If it does not consider the explanatory statement to be in an appropriate form, the court may choose not to order the convening of the target's shareholder meeting(s). This does not however mean that the court will approve the explanatory statement at the Convening Hearing. Instead it will remain open to any person affected by the scheme to raise issues as to the statement's adequacy at the Sanction Hearing.

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