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ACQUISITIONS EFFECTED BY MERGERS, AMALGAMATIONS & SCHEMES OF ARRANGEMENTS

by Matthew Ebbs-Brewer, Seth Darrell, Kendall Evans and Gary Harris

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Bermuda is known as a first class centre for international business. This past year has seen a great deal of merger and acquisition activity for Bermuda headquartered (and often listed on an international stock exchange) companies in the (re)insurance space with their involvement in a series of significant business combinations and acquisitions. This has provided an opportunity to explore the ways in which such transactions can be effected by considering recent market trends to highlight matters that are commonly of interest or concern to clients and onshore counsel. These principles are equally applicable irrespective of one's involvement in the (re)insurance sector.

The body of Bermuda's law on companies, including the provisions through which business combinations and acquisitions of the same are effected, is contained in the Companies Act 1981, as amended (Companies Act). The Companies Act based many of its provisions on the Companies Act 1948 of the United Kingdom and so, English lawyers and those from other common law jurisdictions tend to feel a welcome familiarity with the way in which Bermuda's company law is applied. However, there are some differences and additions, including the provisions that form the focus of this article, which were imported from Canada and allow for the merger or amalgamation of Bermuda companies. Transactions may also be structured by way of a scheme of arrangement which is, as a matter of law, a compromise or arrangement between a company and either its creditors or its members.

Transactions that have taken place in the market have included both those where the fundamental commercial principle is that one group wishes to acquire or "take over" another group and those which are intended to be more of a consolidation of two existing players or a "merger of equals".

Whilst the commercial principles of a transaction may be readily identifiable and distinguishable, Bermuda company law is not prescriptive as to how that commercial reality is to be effected. The parties to an acquisition may wish to structure their transaction by way of a direct share purchase or a "merger". Context is likely to dictate which method is preferred in a given set of circumstances. By way of example, a share purchase may be preferred where this is resistance from a board to engage in a negotiation with a potential suitor. In contrast, a merger may be preferred where the respective boards are keen to agree to the terms upon which two existing groups will be brought together.

The term "merger" tends to be used as a catch phrase for combinations but, under Bermuda law, whilst they can take place under the merger provisions of the Companies Act, they may also be undertaken pursuant to the amalgamation provisions. The processes to complete either are similar and they share many common provisions in the Companies Act, however, as a technical matter they are quite different.

A merger between two (or more) Bermuda companies is typically effected pursuant to section 104H of the Companies Act and, upon completion, the undertaking, property and liabilities of each is vested in one of those companies which remains as the "surviving company" whilst the remaining company or companies cease to exist. The merger provisions are a relatively new addition to Bermuda law and introduced in large part due to a call to be able to effect US style combinations.

An amalgamation between two (or more) Bermuda companies is instead typically effected pursuant to section 104 of the Companies Act and, upon completion, each of the companies become one "amalgamated company" and the undertaking, property and liabilities of each becomes the property of the amalgamated company. A useful way of envisaging an amalgamation is to view the existing companies as tributaries which flow into and continue as a single river. In this form of combination, each company continues to exist rather than there being a lone "survivor".

For our part in Bermuda we tend, although there may be certain instances as addressed more fully below where there may be a preference, to be indifferent, from a purely legal perspective, as to whether a transaction should be structured as a merger or an amalgamation under the Companies Act. From a commercial perspective, we have seen a desire to proceed with an amalgamation when seeking to structure a business combination as a "merger amongst equals", given that neither company is deemed to be the survivor. Conversely, in a situation where one party is for all intents and purposes seeking to acquire the other, a merger may be the preferred choice. Onshore counsel may also have a preference for the resultant company to be a sole survivor or an amalgamated entity so as to be in-line with the treatment available and expected by shareholders familiar with their local tax rules. Whilst not definitive, and there may be variations, we have seen a trend for US transactions preferring to proceed by way of merger whilst common law jurisdictions such as Canada electing to proceed by way of amalgamation.

In order to effect a merger or an amalgamation, the terms of the transaction must be approved by the shareholders of the company. In practice, there are often two agreements in the context of an amalgamation or merger. The first is a more fulsome transaction agreement, often subject to the law of the parties' onshore counsel or the jurisdiction in which the company is listed, which sets out the terms upon which the entire transaction is to be completed and includes comprehensive warranties, indemnities, conditions precedent, deal protection mechanisms and such other terms commonly included in business combinations and acquisitions the often called "Agreement and Plan of Merger/Amalgamation" (in the case of US transactions) or "Implementation Agreement" (in the case of English law transactions and, in either case, referred to in this article as the "main agreement"). In conjunction, there is a statutory agreement which sets out that which is required to be approved by the shareholders under the Companies Act – the so-called "statutory merger/amalgamation agreement" (again, as the case may be and referred to in this article as the statutory agreement).

In terms of process, the main agreement is the document that is the subject of intense negotiation, which is not surprising given its content. Many of the sensitive terms will be discussed in future articles in this series.

The statutory agreement includes those provisions which are required under the Companies Act and which will, in practice, have largely been agreed upon and set out in the main agreement.

Once the form of the main agreement is agreed, the boards of each party typically convene to approve the transaction and resolve in due course to obtain the approval of the shareholders. The main agreement is then executed by the parties with shareholder approvals being obtained subsequently but before the execution of the statutory merger agreement and the related submission to register the combination with the Registrar of Companies in Bermuda. The considerations that the board must take into account when seeking to obtain the approval of the shareholders will also be considered in future parts of this series.

Given the need to obtain shareholder approval, the bye-laws (which regulate the administration of a Bermuda company) must be considered in order to understand the applicable thresholds that must be passed. The requisite approval under the Companies Act is the affirmative vote of 75% of those voting at the meeting, the quorum for which is two persons at least holding or representing by proxy more than one-third of the issued shares of the company. Importantly, holders of shares that otherwise do not carry the right to vote are entitled to vote upon the transaction. Failure to appreciate this point at the outset can cause confusion when drafting the provisions of the main agreement when dealing with the procurement of shareholder meetings. A separate class vote may be required where the terms of the transaction would result in a variation of rights of one or more classes of shareholders.

The statutory threshold of 75% can be a high threshold and it may in certain circumstances prove difficult to solicit responses from retail investors or preferred shareholders. It is often seen as an advantage in order to secure the completion of a transaction if one specifies a lower threshold in the relevant company's bye-laws (often 50%). This is often so as not to thwart a potential merger or at least avoid making a potential suitor less willing to commit time and resources to a deal which it considers approval will be difficult to obtain (unless of course such an appearance is actually desired in the context of deal protection mechanisms which will be discussed later in the series). At this point, it is worth noting that as the merger provisions were inserted a number of years after those providing for amalgamations, bye-laws of older companies may only include a lower voting threshold in respect of the latter. This would therefore be an instance where a Bermuda law justification would exist for electing to proceed by way of amalgamation over a merger. It may be possible to provide for a lower threshold in conjunction with seeking approval for a given transaction.

When seeking the approval of the shareholders, notice convening the meeting of such shareholders must be given not less than five days before the date of the meeting (subject to consent to short notice) and must include a statement of what the directors of a company have determined the fair value of their shareholders shares to be. Shareholders have a right, if they do not vote in favour of the merger, to apply to the Bermuda courts to have them appraise the value of their shares. It should be noted that these appraisal rights do not carry the ability to prevent the transaction and if the parties decide to proceed they would simply be required to pay the difference, if any, at a later date should it be determined that a dissenting shareholder had indeed received less than fair value for their shares. It is open to the parties to delay proceeding with the merger until the value of the shares has been appraised or even abandon the transaction. It may also be the case that the main agreement includes provisions that provide for such abandonment in the event that there are a number of dissenting shareholders over a given threshold.

Having decided to proceed and once the certificate of merger or amalgamation, as the case may be, has been obtained from the Registrar of Companies, the parties will have completed the legal requirements to effect the combination under Bermuda law are then free to move forward as they seek to realise the commercial objectives of entering into the transaction in the first place. However, as this series of articles is intended to show, there are a number of practical considerations that must be taken into account in order to cement the completion of a transaction.

This article has been written by:

Bermuda
Matthew Ebbs-Brewer
Associate
+1 441 298 3226
mebrewer@applebyglobal.com

Bermuda
Seth Darrell
Associate
+1 441 298 3285
scdarrell@applebyglobal.com

Bermuda
Kendall Evans
Associate
+1 441 298 3590
kevans@applebyglobal.com

Bermuda
Gary Harris
Associate
+1 441 298 3249
gcharris@applebyglobal.com

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