WATSON FARLEY & WILLIAMS

DEVELOPMENTS IN THE LONDON LISTING MARKETS: CHANGES TO UK TAKEOVER CODE AND BUDGET MEASURES AFFECTING AIM

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We welcome in 2025 with a new series of articles on developments in the London listing markets. In this first one, we focus on significant changes to the UK Takeover Code (the "Code") which will reduce the types of companies subject to the Code, as well as the tax measures announced in the Autumn Budget which directly affect AIM.

Our previous articles in relation to developments in the London listing markets can be found **here**.

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CHANGES TO THE SCOPE OF COMPANIES SUBJECT TO THE UK TAKEOVER CODE

On 6 November 2024, the Panel on Takeovers and Mergers (the "Panel") published a response statement to its April 2024 consultation paper, confirming amendments to the Code which will narrow the scope of the companies to which the Code will apply from 3 February 2025 (subject to transitional arrangements). The amendments will refocus the application of the Code on companies which are registered in the UK, Channel Islands or Isle of Man ("UK registered" companies) and whose securities are (or were recently) admitted to trading in one of those jurisdictions.

Background

The Code contains the statutory rules and general principles that regulate the conduct of UK public takeovers. It is designed to promote, as part of a wider regulatory regime, the integrity of UK financial markets, both by ensuring that offeree company shareholders are given the opportunity to decide on the merits of a takeover and afforded equivalent treatment and by preventing the offeree company from taking certain frustrating actions.

Application of the Code until 3 February 2025

Currently, the Code applies to offers for:

1. UK registered companies whose securities are admitted to trading on a UK regulated market (e.g. the Main Market of the London Stock Exchange or the AQSE Main Market), a UK multilateral trading facility (e.g. AIM or the AQSE Growth Market), or a stock exchange in the Channel Islands or the Isle of Man (“UK quoted” companies); and

2. UK registered companies which are considered by the Panel to have their place of central management and control in the UK, Channel Islands or Isle of Man (i.e. are “UK resident”), and are either:

(i) public companies which are not UK quoted; or
(ii) private companies meeting certain criteria (e.g. were UK quoted or have filed a prospectus during the previous 10 years or have been subject to specified marketing or publicity arrangements).

Changes to the scope of the Code

The amendments to the Code will take effect on 3 February 2025 (the “implementation date”), which marks the start of a two-year transition period that will end on 2 February 2027 (the “transition period”).

Subject to the transitional arrangements described below, the scope of the Code will be narrowed so that from 3 February 2025 it only applies to a company if, on the relevant date, the company is UK registered and either:

- the company is UK quoted; or
- the company was UK quoted at any time during the two years prior to the relevant date,

in each case regardless of whether the company is UK resident.

The “relevant date” for these purposes (and elsewhere in this article) is the date on which an announcement is made of a proposed or possible offer for the company or the date on which some other event occurs in relation to the company which has significance under the Code.

Which companies will no longer be caught?

Subject to the transitional arrangements described below, and provided that the company had not been UK quoted at any time during the two years prior to the relevant date, the Code will cease to apply to the following UK registered companies:

> "The amendments to the Code will take effect on 3 February 2025, which marks the start of a two-year transition period that will end on 2 February 2027."

- a public or private company which ceased to be UK quoted more than two years prior to the relevant date;
- a public or private company whose securities are, or were previously, admitted to trading solely on an overseas market;
- a public or private company whose securities are, or were previously, traded using a matched bargain facility, such as Asset Match or JP Jenkins;
- any other public company which is not UK quoted; and

- a private company which filed a prospectus at any time during the 10 years prior to the relevant date.

The Panel has also confirmed that the Code will not apply to a UK registered company which is not and has not recently been UK quoted solely by virtue of its securities or other interests being traded using another platform, such as:

- a Private Intermittent Securities and Capital Exchange System (or PISCES);
- a private market (such as TISE Private Markets); or
- a secondary market of a crowdfunding platform (such as the Seedrs Secondary Market).

The Code will also explicitly state that it does not apply to a company with a sole beneficial owner (codifying existing practice).

Transitional arrangements

In recognition that companies to which the Code will cease to apply ("transition companies") and their shareholders will need time to consider the implications of no longer benefiting from the protection of the Code and any actions they may wish to take, the changes will be prefaced with a two-year transition period. The transitional arrangements are set out in a Transitional Appendix which will be introduced into the Code from 3 February 2025.

During the transition period, application of the Code will continue to be a relevant consideration for a transition company in the same way as it was immediately before the implementation date.

Accordingly, it will be key for a company to determine (i) if it is a transition company, which will depend on the company's status immediately prior to the implementation date, i.e. on 2 February 2025; and (ii) if so, whether the Code applies to it in respect of a specific transaction during the transition period, which will depend on the circumstances of the company on the relevant date.

Is a company a transition company?

A company will be a transition company if it either:

- satisfies the description at paragraph (2) above on 2 February 2025; or
- would satisfy the description at paragraph (2) above on 2 February 2025 **if it had been UK resident at that date**.

As a result, a company that is not currently subject to the Code because it is not UK resident may be classed as a transition company.

Is a transition company subject to the Code?

Whether the Code applies to a transition company in respect of a specific transaction during the transition period will depend on the circumstances at the relevant date, including:

- whether the company is UK resident at the relevant date; and

- in the case of a private company that was in a 10-year run-off period immediately before the implementation date, whether any of that period remains outstanding.

Therefore, if the residency of a transition company changes during the transition period, it may become subject to the Code where it previously was not in respect of a specific transaction taking place during the transition period or, conversely, no longer be subject to the Code where it previously was.

The Panel has published a helpful **table** and two flow charts in Appendices D and E to the **response statement** to guide companies tasked with determining whether they will be considered a transition company and/or a Code company during the transition period.

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Run-off period for companies ceasing to be UK quoted

In addition, a UK registered company that is UK quoted and thus subject to the Code on 2 February 2025, but ceases to be UK quoted during the transition period, will continue to be subject to the Code for two years after it ceases to be UK quoted, regardless of whether it satisfies the residency test.

Waivers

The Panel may, where it would be inappropriate or disproportionate for the Code to apply to a company in relation to a particular transaction, grant a waiver from the application of some or all provisions of the Code in respect of transition companies or companies which cease to be UK quoted. However, the Panel has clarified that a waiver is unlikely to be granted simply because a company has ceased to be UK quoted within the previous two years, since it believes that the Code should continue to apply for a run-off period to companies which cease to be UK quoted, even if their securities become admitted to trading on an overseas exchange.

Commentary

These changes are welcome as they will provide greater clarity and certainty as to the companies that are subject to the Code and ease the regulatory requirements on unquoted public and private UK registered companies and those only quoted overseas which will cease to be subject to the Code.

However, companies to which the Code will cease to apply ought to be proactive, during the transition period, in considering the arrangements and actions they may wish to adopt and/or take to afford their shareholders some of the protections they currently benefit from under the Code and to reflect the changes taking effect. These include, for example:

- a company making itself subject to the Code or an alternative regulator of takeovers (e.g. by admitting its securities to trading on an appropriate market);

"Companies to which the Code will cease to apply ought to be proactive, during the transition period, in considering the arrangements and actions they may wish to adopt and/or take."

- amendments to the company's articles to introduce provisions equivalent to certain aspects of the Code (e.g. a requirement for a shareholder who obtains or consolidates control to make a mandatory offer on similar terms to an offer required under Rule 9 of the Code);
- arrangements for shareholders to exit their investment if they do not wish to be shareholders in the company without the protections afforded by the Code; and
- updating public filings (e.g. filings stating that a company is subject to the Code).

AUTUMN BUDGET 2024

The Autumn Budget of 2024 has been described as the most consequential by a British government in over two decades. Here we focus on the impact of the Chancellor's measures on AIM.

Whilst AIM peaked at 1694 companies in 2007, this number has since dwindled to 685 in December 2024, its lowest level since 2001, with only 15 companies being admitted to AIM in 2024 through IPO, introduction or transfer to AIM. Set against a backdrop of a steady stream of de-listings, with 44 companies departing since the start of July 2024, this lethargy has not been helped by the new Labour government's commitment to balancing the nation's books through tax increases. Notably, its targeting of the 100% rate of relief from inheritance tax applicable to shares held on AIM for at least two years (known as Business Property Relief), which was one of the benefits of investing in shares on the junior market.

Changes to relief rate

In her budget statement, Chancellor Rachel Reeves announced that a new rate of 50% for inheritance tax relief for shares on AIM will apply in all circumstances from 6 April 2026. This represents a halving of the current rate of relief, taking the effective rate of inheritance tax to 20%.

Despite the reduction to the relief, the nightmare scenario that many investors feared of a wholesale abolition, which would have set the effective inheritance tax rate at the standard 40% for AIM shares, has been averted. Octopus Investments, one of the major providers of AIM inheritance tax portfolios, advised investors that they need take no action in the wake of the Budget.

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AIM also avoided a widely rumoured scrapping of the capital gains uplift in the base cost applicable to inherited assets benefiting from business relief. This uplift means that, for the purposes of capital gains tax, the base cost of assets in an estate are determined at the date of death, as opposed to the date of acquisition by the deceased – the value is uplifted. Combined with the 50% rate of relief, this has preserved the so-called inheritance tax "double dip" to some extent.

This is particularly welcome considering the accompanying rises in capital gains tax to 18% and 24% for basic and higher rate taxpayers respectively. Moreover, the reduced rate of capital gains tax available under Investors' Relief, applicable to qualifying disposals of shares in unlisted trading companies (which includes those held on AIM), is also increasing to 14% in April 2025, followed by a further rise to 18% in April 2026.

The Chancellor also announced that 'inherited pensions' will become subject to inheritance tax from April 2027 at the standard rate of 40%. Accordingly, this could make the 20% rate on AIM shares attractive in comparison.

The exemption from stamp duty for stock held on AIM has also been retained.

Energy provisions

Energy is a crucial sector for AIM. As regards the oil and gas industry, the Budget increased the Energy Profits Levy rate by 3% to 38%, removed the Energy Profits Levy Investment Allowance altogether, and cut the Decarbonisation Investment Allowance rate from 80% to 66%.

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Conversely, in respect of clean energy, the Budget allocated £3.9bn towards funding carbon capture and storage. Moreover, oil and gas companies are being offered relief payments for assets sold for carbon capture and storage (this income not being subject to the Energy Profits Levy). £200m has also been ringfenced for investment in on-street charging points for electric vehicles.

Whilst the confirmation of these changes has brought new-found certainty to the energy companies on AIM, there is a risk that profitability in oil and gas production could be held back due to these measures. However, there will still be tax losses that AIM companies can utilise.

Commentary

There has been some criticism of the Budget as a missed opportunity to go further in proactively providing support for smaller companies, tackling the issues of low valuations, low liquidity and a limited appetite to support fundraisings.

However, overall, the outcome is ultimately positive for AIM, with fears of its demise being overblown. These new measures restore some certainty to the junior market. Indeed, in the immediate aftermath of the Budget, the FTSE AIM 100 index shot up by around 4%, albeit it has since fallen back slightly.

In the context of expected falling interest rates and a new government that, in the words of the Chancellor, wants to 'invest, invest, invest' in a dash for growth, it is hoped that the retained tax incentive signals that AIM remains an attractive venue for global companies to list, particularly given the flexibility provided to growing companies through its lighter regulatory touch relative to other UK markets.

CONCLUSION

With the continuing volatility in the UK markets, it is hoped that the measures outlined here will bring some degree of stability and certainty and that this will be further helped by other reforms in the pipeline, such as introduction of the new rules relating to prospectuses and making public offers. These are expected to be finalised by the end of H1 2025 (with a further period before the rules take effect) and aim to make fundraisings and admission to various London markets simpler and a more attractive option.

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