Linklaters

An in-depth study into liability management transactions: Session 2 - Tender offers and on-market buybacks

May 2020

Our five part liability management webinar series – your questions answered

With the recent increase in liability management activity in Asia, we are pleased to present our five part webinar series which will aim to provide you with an in-depth study into liability management transactions. In this series, we will cover a range of topics including a number of commercial and legal questions frequently asked by bankers and issuers on liability management transactions – for example:

> Can we undertake a third party tender offer or exchange offer?

> **How do we locate bondholders?**

> **Can we speak to bondholders prior to launch and undertake pre-sounding? What can and can't we say?**

> **Can the issuer continue to buy back bonds in the open market ahead of launch of a tender offer?**

> When and why would an issuer want to undertake (a) a tender and exchange, (b) a tender and consent or (c) an exchange and consent?

> Can we secure "anchor" bondholder support ahead of launching a tender offer, exchange offer or consent solicitation?

> **Can we exclude U.S. bondholders even where the existing bonds are cleared through DTC?**

> What happens when a disgruntled bondholder challenges the tender offer, exchange offer or consent solicitation shortly after launch?

> What is the difference between an exchange offer and extending the maturity date of existing bonds?

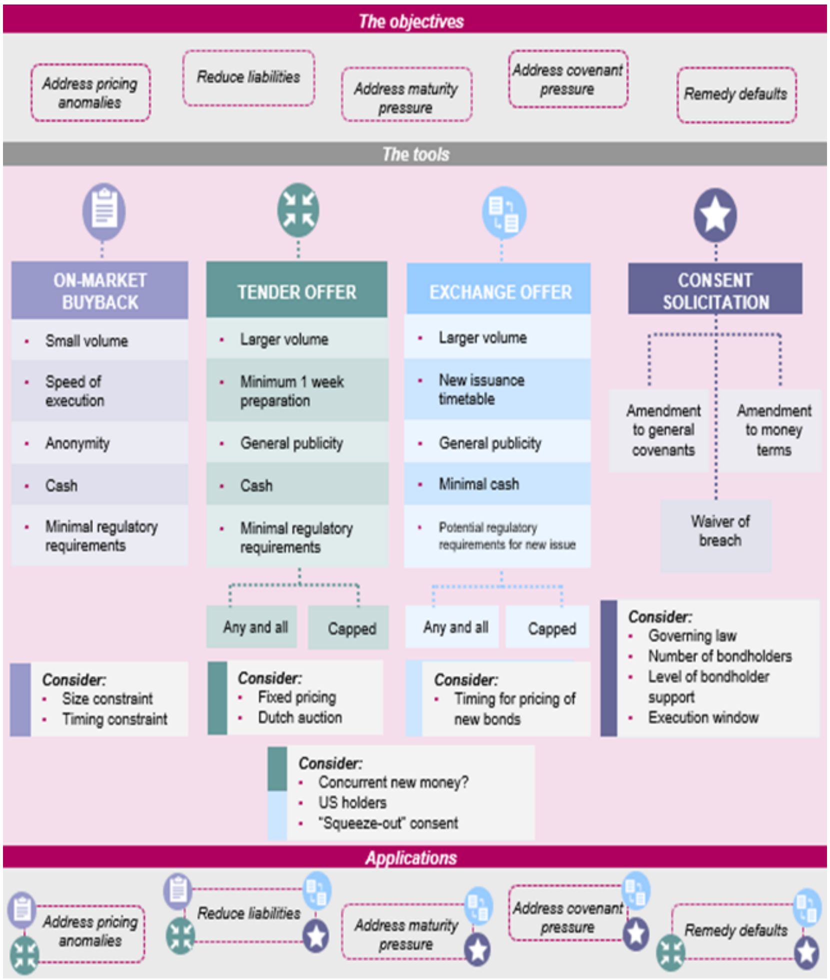
> **What happens if the issuer's financials will be published during the offer period?**

Ranked No. 1 for Managers' Legal Counsel (*Debtwire 2019 APAC (ex-Japan) USD High Yield Bonds League Table*)

Ranked No. 1 for Issuer's Legal Counsel (*Bloomberg 2019 Asia (ex-Japan) Issuer G3 Currency Bonds League Table*)

Ranked No. 1 for Managers' Legal Counsel (*Bloomberg 2019 Asia (ex-Japan) Issuer G3 Currency Bonds League Table*)

The road map below illustrates some of the key areas which we will be exploring in our five part webinar series.



In Session 1 held on 28 April, we discussed how liability management presents a hugely valuable tool for issuers – whether it be to optimise their balance sheets and capital structures, manage relationships with investors, react to new business and market developments, respond to changes in the regulatory landscape or other commercial and legal drivers.

This client note is a follow-up to Session 2 that was held on 5 May 2020 for our debt capital markets clients.

We hope you find our webinar series and corresponding client notes useful. As always, we encourage you to get in touch with us and speak to your usual Linklaters' contacts if you have any questions.

Introduction

In this Session 2, we provide an in-depth discussion on tender offers and on-market buybacks, including:

- Potential legal restrictions;
- Disclosure obligations and inside information concerns;
- Identifying bondholders and dealing with U.S. holders;
- Minimum offer periods; and
- Combined tender offers and new bond issuances.

In this series, we have focussed primarily on liability management conducted outside of the United States although our fifth and final webinar and client note will examine U.S. issues on liability management transactions.

On-market buybacks

Issuers will often look to undertake an on-market buyback where they are aiming to retire a small amount of bonds discreetly from the open market. Such buybacks are frequently opportunistic, with the goal being to repurchase a relatively small amount at a low premium to secondary price levels, by taking advantage of pricing or market anomalies. The pricing and other terms of the on-market buyback will typically be privately negotiated between the issuer (often acting through a financial intermediary) and the seller.

Tender offers

A tender offer is an approach by an issuer to all or substantially all its bondholders to buy back its bonds for cash. The structure of the tender offer depends on the commercial objectives of the issuer – for example:

- Whether the issuer is looking to repurchase as much as possible from the market versus a capped amount; and
- Whether the issuer has a clear idea of the price it is willing to offer to investors versus asking investors to submit offer prices. The latter is used where the issuer is looking to repurchase a capped amount (as a Dutch auction mechanism looks to create some price tension in the tender offer) and may be particularly useful where the secondary market price is relatively volatile or if the issuer is otherwise less willing to set a fixed price at the time of launch.

Key Issues

Review the bond terms

You should always check the terms and conditions of the bonds. While bonds in Asia will typically allow issuers to conduct on-market buybacks and tender offers, this is not always the case. In particular, for issuers with high yield bonds, bond repurchase through on-market buybacks or tender offers will often be treated as a Restricted Payment and therefore would be restricted unless there was an available Restricted Payment exception.

In addition, the terms and conditions may not allow the issuer to resale the repurchased bonds. It is quite common for bonds in Asia to require all repurchased bonds to be promptly cancelled.

Dealing Disclosure Requirements

Most bonds will either be listed on a stock exchange or are issued by an issuer whose shares are listed on a stock exchange. Accordingly, before the issuer deals in any bonds (whether by an on-market buyback or tender offer) the relevant stock exchange requirements should be considered carefully.

As a general observation, an on-market buyback may not require public disclosure provided that (i) the amount of bonds repurchased does not exceed the prescribed threshold under the relevant stock exchange listing rules (for example, for SEHK: 10% and every subsequent 5% interval of the original issue size; and for SGX-ST: every 5% of the total principal amount, calculated based on the principal amount at the time of initial listing) and (ii) the buyback itself would not be considered price sensitive information under the relevant stock exchange's insider dealing (or other equivalent) rules. On the other hand, for tender offers, public disclosure at launch, final tender acceptances and completion will be required in most circumstances as the offer is being made to all or substantially all investors.

The issues around inside information and insider dealing can be complicated and specific legal advice should always be sought. Broadly, inside information is specific information that is not generally known to the market which would likely materially affect the price of the bonds. While there is no exhaustive list of what constitutes inside information, the following questions should be considered:

> Is the bond repurchase itself inside information?

> Does the issuer have financial information that is not public? Are the upcoming financial results in line with market expectations?

> Is there any material restructuring, merger and acquisition activity, change in business?

If the Issuer has securities which are admitted to trading on a European regulated market or multilateral trading facility or organised trading facility, the EU Market Abuse Regulation (MAR) requirements should also be considered.

Bondholder identification

When planning a tender offer or other liability management exercise, you may wish to identify the current bondholders in advance. Although Euroclear and Clearstream keep investors' details confidential, it is possible to conduct jurisdictional surveys to ascertain the location of investors, number of accounts and concentration of holdings. For example, it is possible to tell from jurisdictional surveys if current investors are based in Asia, U.S. or Europe and the investor type (institutional investors versus private bank clients). As part of preparation and planning for a tender offer, you may wish to know broadly, the jurisdictions where holders are located.

There are service providers who provide bondholder identification services. Such services include:

- Basic services to ascertain the countries where the custodians (and ultimate holders) are located. The cost is around USD500 – 800 per ISIN and the process is relatively quick with the information typically available within five business days.
- Advanced services to try to determine the current list of bondholders and their key decision makers. This process is more complicated and involves trying to trace the ownership from the original investor allocation lists as well as requesting investors to voluntary disclose their identities through the clearing systems. Depending on the advanced services needed, the cost is around USD10,000 – USD15,000 per ISIN and the process takes around two to three weeks.

Excluding U.S. bondholders

Tender offers conducted by Asian issuers often seek to exclude U.S. holders to avoid the application of the tender offer rules under U.S. securities laws. If only a small portion of bonds are held by U.S. holders, structuring the tender offer to comply with U.S. tender offer rules may unnecessarily complicate the process and increase costs for the issuer.

For Asian issuers that have issued bonds on a Rule 144A basis, this may present a challenge as the holdings by U.S. holders may be significant. However, even in these circumstances, it may be possible to exclude the U.S. holders by carefully structuring the tender offer to ensure it is not transmitted into the U.S. For example, the tender offer should only be disseminated through Euroclear and Clearstream and not DTC and investors will need to confirm they are not U.S. holders. The exact way in which this structuring is achieved will also depend on the way in which the original issuance was cleared – there are a variety of ways in which a Rule 144A offering can be cleared, involving DTC and/or Euroclear and Clearstream.

In addition, where bonds are held through DTC, even if the tender offer is not disseminated through DTC, there will be certain processes involving DTC, such as certain notices, which will still need to be sent to bondholders through DTC. The key point will be to ensure that such processes involving DTC only take place after the tender offer period has expired.

It should be noted that excluding U.S. bondholders is not something that is always possible on liability management transactions, in particular, consent solicitations. In Session 5 of our webinar series, we explore this point as well as other U.S. securities laws considerations in the context of tenders offers and liability management more broadly.

Time is of the essence

Minimum offer periods

Tender offers carried out through Euroclear and Clearstream are required to be open for a minimum of 5 business days. This is to ensure that all bondholders are given an adequate opportunity to take action on any information received through Euroclear and Clearstream. If the tender offer is subject to U.S. tender offer rules, the tender offer period must be a minimum of 20 business days and at least a further 10 business days if there is a change in the material terms of the tender offer.

The issuer when structuring early bird incentives (such as early bird payments) to encourage early bondholder acceptances should also carefully consider the time period for early bird incentives. In certain circumstances, it may be more appropriate to structure the early bird incentives so that they are conducted outside the clearing systems.

Accelerated tender offers

For convertible bonds and exchangeable bonds, where the bonds are typically held by a relatively small number of accounts and investors are accustomed to make investment decisions on an accelerated basis or bonds issued by sovereign credits, where most investors buy-to-hold, it may be possible to conduct accelerated tender offers by directly contacting all or substantially investors outside the clearing systems. In an accelerated tender offer, the dealer manager would coordinate the tender offer, directly contact the investors and process and settle the payment of the tender offer price and transfer of the bonds – effectively replacing the role the clearing systems would typically play. The offer periods for accelerated tender offers often do not exceed more than 1 business day.

Accelerated tender offers are generally not suitable for other corporate bonds. Some additional risks associated with accelerated tender offers include:

- No formal disclosure document is prepared so it is important to make sure there is no disparity of information being disseminated;
- Parties will need to be reasonably comfortable that it will be possible to contact all or substantially all of the investors (as well as consider whether the issuer would extend the offer to any bondholders who missed the initial offer); and
- Settlement of the accelerated tender offer will require the dealer manager to act as settlement bank and this may involve increased risk for the dealer manager (e.g. in the case of failed trades).

Other tender offer structures

Tenders offers with new bond issuances

Given long term interest rates are expected to continue to remain at historic lows for some time, issuers are also looking for ways of combining tender offers with new bond issuances. This effectively creates a “synthetic” exchange offer but may be simpler to execute. For the issuer, a successful “synthetic” exchange allows it to proactively extend its debt maturity profile as well as lower its overall funding costs. In a combined tender offer and new bond issuance transaction, the tender offer and new bond issuance will typically be linked so that the new bonds will need to have been successfully issued before the tender offer price is paid over to the holders. Issuers may also choose to sweeten the deal for holders of the existing bonds participating in the tender offer by granting such investors priority allocation in the new bond issuance.

When undertaking a combined tender offer with new bond issuance, there are a few important considerations:

- Ensure the tender offer and new bond issue commercial objectives are aligned (for example, is it more important for the issuer to maximise the tender offer acceptance rate or the new bond issuance size);
- Consider if there are any legal restrictions from explicitly linking the tender offer and new bond issuance (for example, in certain circumstances it may not be possible to give investors priority allocation codes); and
- Consider if the issuer has sufficient funds (or has arranged bridge financing) to settle the tender offer. Whilst it is typical for the new bond issue and the tender offer to be settled on the same day so that investors have not "doubled" their exposure to the issuer, the new bond proceeds will often not be available to be settle the tender offer price before the relevant clearing system payment cut-off deadlines.

Stay tuned: 12 May 2020 - our next webinar session on exchange offers

We welcome you to join us for our next session on exchange offers where we will take an in-depth look into:

- The reasons for conducting exchange offers;
- How to price the new bonds in an exchange offer;
- The interaction between the exchange offer and the new bond issuance including timetable considerations; and
- The difference between conducting an exchange offer versus an extension of the maturity date of the existing bonds.

Contacts

Terence Lau
Partner, Hong Kong SAR
Tel: (+852) 2842 4182
terence.lau@linklaters.com

Hanwen Yu
Partner, Hong Kong SAR
Tel: (+852) 2901 5439
hanwen.yu@linklaters.com

Taiki Ki
Counsel, Hong Kong SAR
Tel: (+852) 2901 5442
taiki.ki@linklaters.com

For general enquiries please contact

Linklaters
11th Floor, Alexandra House
Chater Road
Hong Kong SAR
China

Tel: (+852) 2842 4888
Fax: (+852) 2810 8133/2810 1695

linklaters.com