

# TAKEOVER APPEAL BOARD

## THE WALT DISNEY COMPANY and SKY PLC

### DECISION OF THE TAKEOVER APPEAL BOARD

#### I. Introduction

1. These are the reasons given by the Takeover Appeal Board (“the Board”) for its decision, announced on 15 August 2018, to confirm the Ruling of the Hearings Committee which confirmed the determination of the Panel Executive (“the Executive”) dated 13 July 2018 that the Chain Principle Offer which The Walt Disney Company (“Disney”) would be obliged to make within 28 days of completing its acquisition of Twenty-First Century Fox Inc (“Fox”) should be at the price of £14.00 for each ordinary share in Sky plc (“Sky”), but that that offer need not be made if by then Fox has acquired 100% of the shares in Sky or Comcast Corporation (“Comcast”) or any other third party has acquired more than 50% of such shares.
2. The reasons for the Ruling of the Hearings Committee are annexed to these reasons.

#### II. Takeover Code provisions

3. This section sets out the provisions of the City Code on Takeovers and Mergers (“the Code”) which are directly relevant and also those other provisions which have been relied on before the Board.
4. General Principle 1 states:

**All holders of the securities of an offeree company of the same class must be afforded equivalent treatment; moreover, if a person acquires control of a company, the other holders of securities must be protected.**

5. Rule 9.1 provides:

**9.1 WHEN A MANDATORY OFFER IS REQUIRED AND WHO IS PRIMARILY RESPONSIBLE FOR MAKING IT**

**Except with the consent of the Panel, when:**

- (a) any person acquires, whether by a series of transactions over a period of time or not, an interest in shares which (taken together with shares in which persons acting in concert with him are interested) carry **30% or more of the voting rights of a company; or**

**(b) any person, together with persons acting in concert with him, is interested in shares which in the aggregate carry not less than 30% of the voting rights of a company but does not hold shares carrying more than 50% of such voting rights and such person, or any person acting in concert with him, acquires an interest in any other shares which increases the percentage of shares carrying voting rights in which he is interested,**

**such person shall extend offers, on the basis set out in Rules 9.3, 9.4 and 9.5, to the holders of any class of equity share capital whether voting or non-voting and also to the holders of any class of transferable securities carrying voting rights. Offers for different classes of equity share capital must be comparable; the Panel should be consulted in advance in such cases.**

...

6. Note 8 on Rule 9.1 states what is known as the “Chain Principle”:

*Occasionally, a person or group of persons acting in concert acquiring shares resulting in a holding of over 50% of the voting rights of a company (which need not be a company to which the Code applies) will thereby acquire or consolidate control, as defined in the Code, of a second company because the first company itself is interested, either directly or indirectly through intermediate companies, in a controlling block of shares in the second company, or is interested in shares which, when aggregated with those which the person or group is already interested in, secure or consolidate control of the second company. The Panel will not normally require an offer to be made under this Rule in these circumstances unless either:*

*(a) the interest in shares which the first company has in the second company is significant in relation to the first company. In assessing this, the Panel will take into account a number of factors including, as appropriate, the assets, profits and market values of the respective companies. Relative values of 50% or more will normally be regarded as significant; or*

*(b) securing control of the second company might reasonably be considered to be a significant purpose of acquiring control of the first company.*

*The Panel should be consulted in all cases which may come within the scope of this Note to establish whether, in the circumstances, any obligation arises under this Rule.*

7. Rule 9.5 states:

#### **9.5 CONSIDERATION TO BE OFFERED**

**(a) An offer made under Rule 9 must, in respect of each class of share capital involved, be in cash or accompanied by a cash alternative at not less than the highest price paid by the offeror or any person acting in concert with it for any interest in shares of that class during the 12 months prior to the announcement of that offer. The Panel should be consulted where there is more than one class of share capital involved.**

**(b) If, after an announcement of an offer made under Rule 9 for a class of share capital and before the offer closes for acceptance, the offeror or any person acting in concert with it acquires any interest in shares of that class at**

**above the offer price, it shall increase its offer for that class to not less than the highest price paid for the interest in shares so acquired.**

**(c) In certain circumstances, the Panel may determine that the highest price calculated under paragraphs (a) and (b) should be adjusted. (See Note 3)**

...

8. Note 1 on Rule 9.5 states under the heading “Nature of consideration”:

*When an interest in shares has been acquired for a consideration other than cash, the offer must nevertheless be in cash or be accompanied by a cash alternative of at least equal value, which must be determined by an independent valuation...*

9. Note 3 on Rule 9.5, under the heading “Adjustment of highest price,” sets out a number of circumstances which the Panel may take into account when considering an adjustment of the highest price, and then states:

*The price payable in the circumstances set out above will be the price that is fair and reasonable taking into account all the factors that are relevant to the circumstances...*

### **III. The offers**

10. On 15 December 2016 Fox announced a recommended cash offer for all the remaining shares of Sky at a price of £10.75 per share. The offer was to be implemented by a scheme of arrangement. At the time of the announcement, the price of £10.75 per share represented a premium of some 36% to the share price of Sky on the day before the commencement of the offer period on 9 December 2016.
11. On 14 December 2017 Disney and Fox announced a definitive agreement for Disney to acquire Fox (after a spin-off of certain Fox assets into a new company owned by existing Fox shareholders) on the basis of 0.2745 Disney shares for each Fox share (subject to adjustment for certain tax liabilities). According to Disney’s investor presentation, the consideration payable was worth approximately \$28.00 for each share of Fox.
12. Later on 14 December 2017 the Executive announced (Panel Statement 2017/23) that it would in due course decide whether Disney’s acquisition of Fox (and with it Fox’s 39% stake in Sky) would trigger an obligation on Disney to make a mandatory offer for the remaining shares of Sky under the Chain Principle, which Disney had disputed.
13. On 27 February 2018, Comcast announced that it was considering making an offer for Sky.

14. By Panel Statement 2018/4 issued on 12 April 2018, the Executive announced that it had informed Disney, Fox and Sky of its ruling that, within 28 days of completion of its acquisition of Fox, Disney would be required to make a mandatory offer to the holders of ordinary shares in Sky pursuant to Note 8 on Rule 9.1 of the Code. The basis for the ruling was the Executive's finding that securing control of Sky might reasonably be considered to be a significant purpose of Disney in acquiring control of Fox. The Executive also stated that the mandatory offer had to be at £10.75 in cash for each ordinary share in Sky, that being the price attributed by Disney to Fox's stake in Sky in the consideration payable by Disney for Fox. Disney would not be obliged to make a Chain Principle Offer if, by the due time for making it, Fox had acquired 100% of the ordinary shares of Sky or Comcast or any other third party had acquired more than 50% of the ordinary shares of Sky.
15. On 25 April 2018, Comcast announced a firm intention to make an offer for Sky under Rule 2.7 of the Code at a price of £12.50 per Sky share. That offer was stated to be conditional upon certain regulatory clearances which have since been received, and was also subject to a 50% acceptance condition.
16. On the same day, the independent directors of Sky announced that, in light of Comcast's stated intention to make a higher cash offer, they were withdrawing their recommendation of Fox's offer of 15 December 2016.
17. On 23 May 2018 Comcast announced an interest in acquiring Fox, and on 13 June 2018, Comcast published a proposal to acquire Fox on the same basis as Disney but at a higher price of \$35.00 in cash for each Fox share. On 19 July 2018 Comcast publicly withdrew its interest in acquiring Fox.
18. On 20 June 2018 Disney announced that it had entered into an amended acquisition agreement with Fox under which its offer price increased to approximately \$38.00 per Fox share. This was subject to a collar arrangement which determined the rate at which Disney shares would be exchangeable for shares of Fox by reference to a specified range for the trading price of Disney shares at completion. Fox shareholders were also given the option of electing for cash or stock subject to 50/50 pro-rating.
19. On 28 June 2018 the Executive announced (Panel Statement 2018/7) that it had received diverging views in relation to the impact of the increased price of Disney's acquisition of Fox on the Chain Principle Offer price of £10.75 set by the Executive's

ruling of 12 April 2018. The Executive said that it would make a further announcement in due course.

20. On 11 July 2018, Fox and Sky announced an increased recommended cash offer for Sky of £14.00 per ordinary share, to be implemented by a scheme of arrangement. In that offer announcement, it was said that Disney had provided its consent to the increase in debt that Fox would incur as a result of the increased offer. The announcement also stated that if Disney's acquisition of Fox did not complete due to a failure to obtain regulatory approvals or in certain other limited circumstances, Disney would reimburse Fox the difference between the consideration of £14.00 per share in Sky payable under the Fox recommended offer and £13.00 for each such share. Disney would also pay any interest and fees on such amount.
21. Later on 11 July 2018 Comcast announced an increased recommended offer of £14.75 for each Sky share. Its offer document was published on 13 July 2018.
22. On 13 July 2018 the Executive announced (Panel Statement 2018/9) its ruling that the price at which Disney would be obliged to make a Chain Principle Offer for each ordinary share of Sky within 28 days of its acquisition of Fox should be increased to £14.00 per share unless by then either Fox had acquired 100% of the ordinary shares of Sky, or Comcast or any other third party had acquired more than 50% of the ordinary shares of Sky.
23. On 27 July 2018 the terms for Disney's acquisition of Fox were approved by the shareholders of both companies. As before, the acquisition was to be effected by a merger after a spin-off of certain of Fox's assets into a new company to be owned by existing Fox shareholders.

#### **IV. Ruling of the Hearings Committee**

24. Following publication of the Executive's ruling in Panel Statement 2018/9, the committee of the independent directors of Sky ("the Independent Committee of Sky"), Elliott Advisors (UK) Ltd on behalf of certain Elliott Funds ("Elliott") and shareholders represented by Greenhill & Co International LLP ("Greenhill") asked for the Hearings Committee to be convened to review the Executive's determination of the Chain Principle Offer price and the methodology applied to arrive at it.

25. On 3 August 2018, the Hearings Committee announced its decision (Panel Statement 2018/13) that the Ruling of the Executive was upheld. In its detailed reasons, the Hearings Committee noted that the Code did not stipulate how the price of an offer made pursuant to the Chain Principle was to be calculated. Rule 9.5 of the Code had no direct application because neither Disney nor any person acting in concert with it had purchased shares in Sky during any period relevant for the purposes of the Code.
26. In October 2008 the Takeover Panel Code Committee had considered whether it should propose in a public consultation document that Note 8 on Rule 9.1 be amended to stipulate a method for calculating a Chain Principle Offer price. The proposal under consideration was that the offer for Company C should normally be made at the same percentage premium or discount to the quoted price of the shares of Company B as had been paid by the acquirer (Company A) for the shares in Company B, unless this produced a manifestly unfair result. The Code Committee decided that such an approach would be too simplistic and would in many cases be inappropriate, for example where Company B and Company C were valued on different bases. Accordingly, the Code Committee concluded that the Takeover Panel's policy on setting a Chain Principle Offer price should be developed on a case by case basis without amending the Code.
27. The Hearings Committee noted that there have been five cases in which an offer had been required under the Chain Principle, but in each case the parties involved reached agreement on the offer price, and none of the cases involved the distinguishing features of the present case, in which Company B (Fox) had substantial assets other than its stake in Company C (Sky); Company B (Fox) would spin-off a portion of its assets before Company A (Disney) completed its acquisition; Company C (Sky) was itself the subject of competing offers from Company B (Fox) and Comcast; Company B's (Fox's) current offer for Company C (Sky) was announced shortly after Company A's (Disney's) revised agreement to acquire Company B (Fox) and was made with Company A's (Disney's) approval and support.
28. The Hearings Committee considered that the last factor was particularly significant because it justified viewing Fox's current offer for Sky, if not as a proxy offer by Disney, then at least as an offer made at a price which indicated the value attributed by

Disney to consolidating control of Sky in the context of Comcast's competing offer of £12.50 per ordinary share.

29. The Hearings Committee upheld the Executive's ruling on the following basis.
30. Rule 9 obliged the party in question to offer to other shareholders the highest price actually paid, not a price which represents the true or fair value of the company's shares at a given time. The Chain Principle Offer price payable under Note 8 should give effect as closely as possible to Rule 9 and its rationale and, by so doing, to General Principle 1 which Rule 9 serves to implement. This meant that, by extension of the traditional application of Rule 9, a Chain Principle Offer price would attempt to reflect the price actually payable by A for B's controlling interest in C, and not some fair or true value of the stake in C assessed at any particular time.
31. The object was to ensure that whatever price was received by the shareholders of B for their shares in C will be offered by A to C's other shareholders, who would then choose whether or not to accept it.
32. Rule 9 was intended to secure equivalent treatment for the shareholders of the offeree; it did not offer a generalised concept of fair treatment. By securing equivalent treatment for the shareholders of an offeree and giving them the opportunity to exit at the best price paid by the acquirer to obtain or consolidate control, Rule 9 ensured that such shareholders are treated fairly.
33. Identifying the price actually paid or attributed by A for B's stake in C did not, however, mean that the Executive was bound to accept the price that A, or A and B together, say is attributable to acquiring the stake in C. An approach which accepted self-certification by A of the price attributed to B's interest in C invited abuse. Any representation of A regarding the price payable for the stake in C would be one piece of evidence which the Executive would take into account, but there would normally be good reasons for not accepting A's say so without testing it against other material. Both Disney and Fox shared a common interest in minimising the Chain Principle Offer price, and to recognise this conflict of interest in attributing a value to the stake in Sky acknowledged commercial reality.
34. But the Executive was experienced in testing the evidence of parties who have an interest in securing a particular outcome.

35. The Executive did not accept Disney's or Fox's say so; and it proceeded to determine objectively what price was actually attributed by Disney and received by Fox's shareholders for Fox's stake in Sky. The principal factors likely to have influenced the Disney board's view of the value of Fox's stake in Sky were Sky's favourable trading performance during the period since the Initial Acquisition Agreement; and the enhanced value of a 39% stake in Sky when Disney was intent upon competing with Comcast for practical control. Fox's 39% stake had a strategic value in moving to 100% ownership and thereby deriving the synergies which would flow from practical control.
36. The Executive had approached the determination of the Chain Principle Offer price objectively. The object of the exercise was to infer from the relevant data what price was actually to be paid by Disney and received by Fox's shareholders for Fox's stake in Sky. The material to enable the Executive to infer the price actually paid by A and received by B for its stake in C would vary from case to case.
37. The core problem was to identify the data or the particular approach which most effectively pointed to the price to be paid by Disney and received by Fox's shareholders for Fox's 39% stake in Sky.
38. The Hearings Committee concluded that the arbitrary nature of the "linear approach" put forward by certain parties ruled it out. There was no reason to believe that by increasing the initial Chain Principle Offer price by a percentage equal to that by which the consideration payable under the Initial Acquisition Agreement increased under the Revised Acquisition Agreement, the value of the stake in Sky (as perceived by Disney) increased precisely in line with the value of Fox's other assets. It was not possible to know the perceived relative increase in value of Fox's assets during the period in question. But the stake in Sky was unlikely to have increased in value precisely in proportion to the increase in value of Fox's other assets.
39. The Hearings Committee also rejected the argument of the Shareholder Group that the matter should be remitted to the Executive with directions to determine the Chain principle Offer with the assistance of expert evidence. Such a procedure might compound rather than alleviate the problem of determining the value attributed by Disney to acquiring Fox's stake in Sky. Expert evidence would itself be open to challenge and would do no more than provide a range of values without removing

scope for substantial argument. The core questions in this case are not amenable to resolution by expert evidence.

40. There was no perfect way to identify the value actually receivable by the shareholders of Fox for their interest in Sky. The most reliable piece of evidence for inferring the value attributed by Disney to Fox's stake in Sky from the consideration payable under the Revised Acquisition Agreement, was the price at which Disney subsequently authorised Fox to bid for the remaining shares of Sky on 11 July 2018. In authorising and supporting this bid, Disney agreed to take on the increase in debt which Fox would have to incur to make the offer. Disney also undertook to indemnify Fox for liabilities attributable to the offer price exceeding £13.00 in the event the acquisition of Fox did not complete for regulatory or for some other specified reasons. The fact that this bid was made three weeks after the announcement of the Revised Acquisition Agreement, did not prevent the offer price authorised and supported by Disney from being a good indication of the value per share in Sky which Disney had previously attributed in agreeing the consideration payable for Fox's assets. The fact that the Fox offer price was authorised and supported shortly after the announcement of the Revised Acquisition Agreement meant that it had real value as evidence for inferring, retrospectively, the value which Disney had attributed to the 39% stake in Sky when agreeing the increased consideration payable under the Revised Acquisition Agreement.
41. Under Rule 9 of the Code, it was the price paid to gain or consolidate a controlling interest which must be offered for the remaining shares. Consistently with this, the Chain Principle Offer price should reflect the price attributed by Disney and received by Fox's shareholders for Fox's 39% stake in Sky. That, in turn, becomes the price which Disney has to offer to the other shareholders of Sky. The price attributed by Disney to acquiring Fox's 39% stake in Sky under the Revised Acquisition Agreement will have been driven by two principal factors, namely, the trading performance of Sky during the period since the Initial Acquisition Agreement and the strategic value to be attached to the 39% stake in circumstances where Disney was intent upon securing effective control of Sky in the face of a competing bid from Comcast.
42. Such considerations were best reflected in the offer price of £14.00 per share authorised and supported by Disney shortly after the Revised Acquisition Agreement had been

announced. A Chain Principle Offer price of £14.00 was considerably higher than Disney's own revised DCF valuation of £11.80 per share and was consistent with the other valuation material available to and considered by the Executive at the time. In addition, the price of £14.00 per share captured the enhanced value of acquiring a 39% stake in Sky in light of the competition for effective control which had developed by the time of the Revised Acquisition Agreement.

## **V. Arguments before the Board**

43. The Board heard representations by or on behalf of the following (all of whom, except Disney, also made written representations): (1) Elliott; (2) Greenhill, representing certain shareholders (Elliott; Davidson Kempner European Partners LLP, and Farallon Capital Europe LLP); (3) the Independent Committee of Sky; (4) Fox; (5) Disney; and (6) the Executive.
44. In summary, they made these points.

### *Elliott*

45. The principle of fair treatment underlies Rule 9 as it does the other provisions of the Code. Rule 9 does not involve an express obligation to pay a fair price, but in attributing a price per share to Fox's holding in Sky, regard must be had not only to the equivalence and protection requirements in General Principle 1, but also to the requirement of fair treatment: Note 3 to Rule 9 refers to "the price that is fair and reasonable taking into account all the factors that are relevant to the circumstances." There is no reason in principle why there should not be an independent valuation. Note 1 to Rule 9.5 envisages an independent valuation in cases where an interest in shares has been acquired for a consideration other than cash.
46. Insufficient regard was had by the Hearings Committee to the fairness or fair treatment principle. The Executive recognised the inherent conflict faced by Disney in attributing value to Fox's stake in Sky, and the need to test any self-certification by Disney against other material.
47. The Executive relied solely on the interrogation of data provided by Disney and Fox. Reliance on fairness opinions provided by advisers to the Disney board was misplaced because they were provided for a different purpose, the fulfilment of directors' fiduciary obligations. The methodology applied by the Executive failed properly to

address Disney's inherent and unavoidable conflict of interest and has, in effect, allowed Disney and Fox to self-certify the Chain Principle Offer price.

48. The £14.00 Fox offer price for Sky did not constitute an independent or objective source and was not an accurate indicator of the value to be attributed by Disney to Fox's stake in Sky.
49. A price per share of £14.00 would allow Disney to acquire control of Sky without affording all shareholders the opportunity to share in the real premium being paid by Disney for control of Sky. Such a result would lead to unfair treatment of the independent shareholders and a failure properly to protect such shareholders.
50. The determination of the Chain Principle must be grounded in objectivity. The approach of regulators in other countries (Hong Kong, Australia and New Zealand, and Sweden) is to have an objective and independent evaluation of the price.
51. The Executive should have sought the benefit of some independent and objective evaluation to provide an objective yardstick for the Executive.
52. The equivalence requirement of Rule 9.5 is a means of satisfying the fairness and protection requirements of the Code. Rule 9.5 requires that the mandatory offeror must offer the highest price paid by it for the offeree's shares during the previous 12 months (irrespective of the number or proportion of the offeree's shares that were the subject of that purchase). It does not simply require the offeror to offer the last price paid, or even a weighted average of prices paid in the last 12 months.
53. Where there have been no purchases by the mandatory offeror, and no such objective evidence of the price the offeror was prepared to pay during that period, the object of the Executive should be to ascertain the price at which the offeree's shareholders would be treated fairly and be adequately protected.
54. A purpose of the mandatory offer provisions of Rule 9 of the Code is that shareholders of a company of which another has acquired control should have an opportunity to exit that company. It is implicit within that purpose that effect is given to the fairness requirement of the Code. The offer of a low price does not meet that fairness requirement and does not meet the purpose of Rule 9.

55. The Executive should have considered the true or fair value of Sky, not as a determinant but as a comparator or yardstick in any determination of whether the Chain Principle Offer price satisfies the fairness and protection requirements. Such a determination would also lead to satisfaction of the requirement of Rule 9.1 of the Code, that all shareholders are granted the opportunity to exit at the same premium price which may have been paid to acquire control.
56. Applying any methodology by reference to objective data points would result in the Chain Principle Offer price being no lower than £15.01 per Sky share.
57. The Executive's ruling should be referred back to the Executive to re-determine the true Chain Principle Offer price, with guidance to adopt a methodology determined by objective data points, which should be as set out in the Greenhill submissions, and taking such independent advice as is considered necessary in order to ensure protection of independent Sky shareholders.

#### *Greenhill*

58. The duty of the Executive is to make the determination of the Chain Principle Offer price in a manner which is objective, and in the spirit of the Code and General Principle 1 in particular.
59. Disney and Fox have a shared interest in minimising the Chain Principle Offer price. Valuation analyses are inherently subjective and significantly influenced by the objectives set out at their creation.
60. The starting point for the Executive should be the financial facts objectively observable by the market and by Sky's minority shareholders: (1) the £10.75 Chain Principle Offer price as per Panel Statement 2018/4 (accepted by the Executive, Sky, Disney and Fox); (2) all values for capital structure, consistent with conventional corporate finance principles, should be normalised such that the £10.75 price per share is translated into a £26 billion enterprise valuation of Sky; (3) Disney's public presentation of its initial offer for Fox as representing an Enterprise Value (EV) of \$66.1 billion (inclusive of Fox's controlling stake in Sky); while its revised offer was presented as an EV of \$85.1 billion, i.e. a 28.7% increase in capital structure neutral valuation.
61. In the absence of clear and compelling evidence which could definitively prove that the increases in value of Fox's stake in Sky over the period were proportionately less than

increases in value of the non-Sky Fox assets, the only logical method would be to apply the same 28.7% enterprise value premium to Fox's stake in Sky – which implies an EV of £33.4 billion for Sky. Arriving at an implied Chain Principle Offer price per share simply requires the deduction of latest value of net debt from this computed EV, before dividing by Sky's shares outstanding.

62. This calculation could be undertaken by the Executive. An independent expert would not be necessary for this aspect of calculation and the outcome would solely use data points observable and clearly understandable in the public domain, which the Executive would have the power to corroborate independently.
63. A linear, pro rata attribution of the increased EV bestowed on Fox by Disney is the clearest, most objective, and inherently transparent basis on which to calculate an appropriate Chain Principle Offer price; it affords due protection to minority shareholders of Sky by treating them in an equivalent manner to Fox, given that a failure to require equality of premium (absent of any definitive evidence to the contrary) would represent a failure to meet this fundamental objective of General Principle 1; and can be calculated by the Executive, without the need for independent experts and without any subjectivity and/or conflicted influences.
64. At the hearing before the Board, Greenhill emphasised that: (1) their clients were prepared to accept the price of £10.75 as a starting point, even though they considered that it was flawed; (2) the figures put forward by Disney and Fox should not be accepted because of the inconsistency between Fox's advocacy of a £12.50 value and the £14.00 bid; (3) a pro rata linear approach was the best approach to calculate the revised Chain Principle Offer price so that it was consistent with the proportionate contribution of the Sky stake to the overall valuation of Fox; and (4) a price of £14.00 implied that the relative contribution of the Fox 39% stake in Sky had decreased in the overall value of the Fox assets.

#### *Independent Committee of Sky*

65. The Board should determine the increased Chain Principle Offer price to be £14.59 per Sky share, because (1) this would ensure the correct application of General Principle 1 and best reflect the rationale of Rule 9.1, rather than relying upon the price at which Disney subsequently authorised Fox to bid for the remaining shares of Sky on 11 July 2018; (2) Disney had agreed to pay a premium price for Fox to acquire its stake in Sky

(being approximately 39% of the issued share capital of Sky and thereby control of Sky for the purposes of the Code) and all shareholders in Sky should be granted the opportunity of an exit at the same premium price as that payable by Disney to Fox to acquire that controlling stake, being an increase to the Chain Principle Offer price proportionate to the increase from the original price of \$28 per Fox share to \$38 per Fox share, as announced on 20 June 2018, namely a 35.7% increase; (3) it is Disney's intention to acquire 100% of Sky and the only reasonable inference to draw from this fact is that Disney must have attributed some strategic and synergistic value to Fox's 39% controlling stake; (4) Disney increased its bid for Fox, including Fox's controlling stake in Sky by an aggregate of 35.7%, and in the light of the performance of the Sky business since December 2017 when compared to the other Fox assets, the Board should dismiss any argument that the controlling stake in Sky should be afforded any lesser increase than a proportionate increase; (5) the price at which Disney subsequently authorised Fox to bid for the remaining shares of Sky on 11 July 2018 is not the most reliable piece of evidence; (6) the proportionate (or so-called linear) approach was a principled and attractive approach, and was based on the most reliable pieces of evidence available; and (7) that approach most effectively pointed to the price to be paid by Disney and received by Fox's shareholders for Fox's 39% stake in Sky.

66. At the hearing before the Board, the Independent Committee of Sky emphasised the need for the independent shareholders' interests in receiving a price which was in accordance with the principle of equivalence in General Principle 1. Reliance on the £14.00 price at which Disney authorised Fox to bid for the remaining shares in Sky on 11 July 2018 was flawed because that approach invited abuse, and £14.00 was not the price agreed to be paid by Disney for Fox's controlling stake in Sky. It was simply evidence of a floor, and not a ceiling. The linear approach most effectively pointed to the proper price. Sky was the "jewel in the crown" and it made no sense not to attribute the increment of value to Sky.

*Fox*

67. The Chain Principle price is the amount per share actually received by Fox's shareholders from Disney for Fox's existing 39% stake in Sky and not a "true" or "fair" value of Sky shares at a given time.

68. The linear increase approach has conceptual and computational difficulties in this case which rule it out as an appropriate method of calculating the Chain Principle Offer price. It does not reflect the actual value being paid by Disney for Fox's 39% stake in Sky. It ignores the fact that a significant proportion of the increase in the Disney/Fox price represents Disney having agreed to pay away more of the US revenue and cost synergies which would be achieved through a combination of the US Disney and Fox assets, none of which related to the existing 39% stake in Sky.
69. The appointment of an independent expert might compound rather than alleviate the problem of determining the value attributed by Disney to Fox's stake in Sky.
70. The valuation methodology advocated by Greenhill would require judgement to be made as to whether a range of factors should be taken into account, which in itself would be a highly speculative and subjective exercise.
71. The correct Chain Principle price is £12.50 per Sky share, being the highest value attributed by both Disney and Fox to Fox's existing 39% stake in Sky at the time of the revised Disney/Fox merger terms. But Fox acknowledged that Disney's support of Fox's £14.00 offer could be said to be an indicator of the value attributed by Disney to Sky shares (although there is clearly a difference between the value for a 39% stake which affords no synergies and the price which a buyer may be prepared to pay for full control of Sky). Fox was prepared to accept the £14.00 Chain Principle price which had been determined by the Executive, and endorsed by the Hearings Committee.
72. An incorrect Chain Principle Offer price would be a damaging intervention in a process which was playing out in the markets.
73. Fox accepts the need for the Disney/Fox attributed value to be scrutinised in the light of the available evidence. The Executive and the Hearings Committee had carried out the exercise properly.

#### *Disney*

74. The Hearings Committee was right to identify the central question as being to identify the data which most effectively pointed to the price to be paid by Disney for Fox's 39% stake in Sky. It was not to identify the true or fair value.

75. Disney did not accept the logic of the £10.75 and £14.00 prices but was prepared to accept the rulings. The correct approach would have been to focus on Disney's internal board discounted cash flow valuation of less than £12. The valuation was prepared with utmost care in the light of the duties of the board and without any attempt to manage the Chain Principle outcome.
76. There were no synergies in owning 39%. Disney accepted the Hearings Committee's confirmation of the £14.00 Chain Principle Offer price for the pragmatic reason that that was Fox's bid and was supported by Disney.
77. The fact that Fox was now offering to other shareholders £14.00 and Comcast was offering £14.75 demonstrated that the other 61% were not suffering any disadvantage.
78. A third party assessment of the value of Sky would be incompatible with the proper application of Rule 9.
79. The linear approach would be arbitrary and would assume that the value of the stake in Sky, as perceived by Disney, increased precisely in line with the value of the other assets which Disney was acquiring, and would ignore such matters as US tax reductions and US cost and revenue synergies. There was a fundamental difference between the value of a 39% stake with no synergy potential and full control. Greenhill's EV approach was flawed by manifest errors, and unjustified assumptions and judgments by including a premium on EV and by misusing the level of net debt.

#### *The Executive*

80. Rule 9 does not require a price to be offered which represents the true or fair value of the offeree company's shares at a given time. The application of Rule 9 satisfies the requirements of equivalent treatment and protection set out in General Principle 1. There is no additional standard that need or should be applied over and above the requirements in Rule 9 in order to give effect to General Principle 1.
81. Note 3 to Rule 9.5 has nothing to do with this case, since it applies only where the equivalent price has to be adjusted. Nor is there anything in the Code which requires an independent valuation: Note 1 to Rule 9.5 is concerned only with the case where the transaction is being made for a consideration other than cash, and the independent valuation is concerned with the non-cash consideration.

82. Rule 9 provides the protection referred to in General Principle 1 for independent shareholders either: (a) by requiring an offer to be made to them at the highest price paid by the new controlling shareholder for shares in the offeree company in the previous 12 months; or (b) in the circumstances of a new share issue leading to a Rule 9 triggering event, by making that issue subject to a vote of independent shareholders.
83. In a Chain Principle situation such as the present case, the requirement of the Code is to determine what proportion of the consideration that Disney will pay to Fox shareholders on completion of the acquisition of Fox is attributable to Fox's Sky shares; and not whether that price is a fair price or a price demonstrating the true value of those Sky shares. The latter is a matter for the independent directors of Sky and their Rule 3 advisers to opine upon in the independent directors' recommendation to Sky shareholders regarding any Disney chain principle offer.
84. The Executive is well-used to applying critical judgement in reviewing materials and interviewing parties who have an obvious economic incentive. Consistent with that experience, as part of its determination of the Offer Price the Executive interrogated materials and individuals objectively, with appropriate scepticism and with the benefit of submissions made by Sky and its shareholders.
85. The Executive did not and does not consider it appropriate to adopt the linear methodology advocated by the Independent Committee of Sky and, in a modified form, by Greenhill. Were a linear approach to be adopted, there were real questions about the appropriate starting point used by the Independent Committee of Sky for its calculation. The consideration per Fox share offered under the original terms of Disney's acquisition of Fox was 0.2745 Disney shares per Fox share. At the time Disney revised the terms of its acquisition, this original consideration was worth \$29.12 per Fox share. As such, on the basis of the revised consideration of \$38 per Fox share (payable 50% in cash and 50% in Disney shares with a collar arrangement), the revised consideration represented an increase of 30.5%, not 35.7% as Sky's calculations presuppose (which use a starting point of \$28 per Fox share).
86. Rule 9 is concerned with seeking to achieve equivalence amongst all shareholders by reference to the price that they receive for their shares. Accordingly, the implications of the debt of the company in which they hold shares is of no relevance.

87. Calculating the enterprise value of the original acquisition of Fox on the basis of \$29.12 per Fox share would imply a percentage increase for the enterprise value of the revised offer of 24.8% as opposed to the 28.7% used by Greenhill.
88. A linear approach is not appropriate and there is no agreement on which linear methodology to use and significant judgements are still necessary to obtain the correct starting and end points, let alone what adjustments should be made.
89. In the present case there was no evidence of a negotiation between Disney and Fox about the Sky stake. It was necessary to cross-check the £14.00 price, which was done by considering the fairness opinion obtained by Disney, and the projections and methodology which were required to be summarised in the S-4 documents filed in the United States, which were in the public domain. None of the parties had criticised the figures.
90. The Executive had at the outset asked Disney what percentage of the total offer price was represented by the Sky valuation on three bases: standalone (i.e. ignoring synergies), standalone and costs synergies, and standalone and cost and revenue synergies. On all three bases the figure was originally below £10.75. At the second stage, the Executive suggested the linear approach to Disney, who provided the internal figures. Until the £14.00 bid there was a variety of possible valuations, but the best bid on the table was £12.50.

## **VI. Conclusions**

### **A. *Question for the Board***

91. On the re-hearing of the case by the Board the question is whether, in the light of the points taken by the various appellants in their grounds of appeal and in their oral submissions at the hearing on 15 August 2018, it should confirm, vary, set aside, annul or replace the ruling of the Hearings Committee dated 3 August 2018 stating reasons why the Chain Principle Offer which Disney would be obliged to make within 28 days of its acquisition of Fox should be at the price of £14.00 for each ordinary share in Sky.

### **B. *Question for the Hearings Committee***

92. The question for the Hearings Committee on its review of the ruling by the Executive was whether the approach of the Executive under Rule 9 of the Code to determine the

Chain Principle Offer price payable by Disney for shares in Sky was right or wrong. It ruled that it was right.

**C. *Matters not in dispute on the hearing of the appeals***

93. The Chain Principle set out in Note 8 on Rule 9.1 of the Code applies in the circumstances of this case.
94. General Principle 1 of the Code applies to the Chain Principle in Note 8 and to the offer price determined under Rule 9 of the Code as that which Disney should be required to make to the holders of ordinary shares in Sky following completion of Disney's acquisition of Fox.
95. The Code does not lay down a detailed approach to be followed by the Panel in determining the share price stated in a Chain Principle Offer.
96. The Code does not expressly require guidance to be obtained by the Executive from an independent expert in order to determine a Chain Principle Offer price.
97. The five previous occasions on which the Panel has required an offer to be made under the Chain Principle were different from the distinguishing features of this case and afford no precedent.
98. As accepted by the Hearings Committee in its ruling, the Executive is experienced in testing the evidence of the parties who have an interest in securing a particular outcome, this being the sort of assessment which it carries out routinely.
99. The determination of the Chain Principle Offer price is to be approached objectively.

**D. *Points taken on the appeals against the ruling of the Hearings Committee***

*1. The true and fair value point.*

100. The argument that the Chain Principle Offer price per share in Sky should be based on a "true" or "fair" or "reasonable" value of the shares in Sky held by Fox is incorrect. It is clear from the provisions of the Code applicable to a Chain Principle Offer that the criteria expressly identified for determining the offer price are those of equivalent treatment and shareholder protection. They are the specific respects in which shareholders in the target company are entitled under the Code to fair treatment.

101. The reference to “fair and reasonable” in Note 3 on Rule 9.5, which was relied upon by Elliott, is of no assistance, since it relates only to the consequences of an adjustment of the highest price, which has no application in the present case.
102. In those circumstances the basis of the price to be stated under Rule 9 in the Chain Principle Offer is the value attributed to and the price paid by Disney for Fox’s share stake in Sky. An assessment of the “fair” or “true” or “reasonable” value of the shares in Sky is not the correct approach to the treatment of Sky shareholders under the Code or on application of the Chain Principle when requiring Disney to make an offer to shareholders in Sky.
103. The Board rejects the contention that the offer price of £14.00 per share was set by the Executive as a result of simply accepting a self-certification process reflecting the perceptions of Disney or Fox or the “fairness opinions” prepared for the benefit of Disney by their advisers, or other “home-grown material” concerned with the interests of the shareholders in Disney.
104. The Board also rejects the contention that the Executive failed to take into account the conflict of interest position between Disney and Fox in attributing a value to Fox’s stake in Sky and the risk of abuse present in such a conflict.
105. The Executive correctly approached the exercise by endeavouring to apply the principle of equivalent treatment of all Sky shareholders, and thereby to (a) establish what proportion of the consideration payable under Disney’s acquisition of Fox was represented by Fox’s 39% stake in Sky; and (b) derive a Chain Principle Offer price per Sky share based on the principle of equivalent treatment. The Executive therefore made enquiries of Fox and Disney in order to determine whether in the negotiation of the purchase of Fox, any price per share had been attributed to Fox’s shareholding in Sky. It then examined whether there was other evidence which indicated an agreement between Disney and Fox on a price per share for Fox’s shareholding in Sky, and in particular examined the valuation materials which were prepared to support Disney’s offer for Fox. That approach resulted in the original Chain Principle Offer price of £10.75 per Sky ordinary share, and the same methodology was applied in arriving at the revised price of £14.00. The Board is satisfied that the Executive was entitled to adopt that approach, and that it did not act wrongly in acting as it did in setting the offer price without the guidance of an independent expert.

106. In the Board's judgment, the offer price was correctly based on a detailed and objective scrutiny by the Executive of all the available evidence (including publicly available evidence) relating to the value attributed by Disney to Fox's 39% stake in Sky. The Board is satisfied that the Executive exercised appropriate rigour in interrogating the parties and weighing the available data and making its assessment of the appropriate price.

2. *The linear increase point and its variants*

107. The proposed alternative approaches that a valuation of the shares in Sky should be reached by applying, as a starting point, a proportionate linear increase in price to the previous offer price for Sky shares determined by the Executive at £10.75 per share, or on some other basis, such as an increase in enterprise value, are not appropriate for setting an offer price in this case.

108. Those alternative approaches are not required or supported by the provisions of the Code as applicable in this case.

109. They are also open to the objection that they do not reflect the price actually paid by Disney for the 39% stake and the value attributed by Disney to the existing stake of Fox in Sky.

110. The Board is satisfied by the submissions on behalf of the Executive and of Fox and by the reasoning of the Hearings Committee that the suggested linear increase approach and its variants face problems as to (a) what would be the appropriate starting point for the calculation of the linear increase and (b) how the calculation of increase in value and of adjustments would be made having regard to the effect of other factors present in the situation. The linear approach depends on adopting a starting point at a different time and in different circumstances than the point at which a value is to be attributed to the value received by Fox shareholders for their stake in Sky. This means that it is open to the objection that it cannot be regarded as an objective measure of the value attributed to the Sky stake at that latter time.

3. *The independent expert point.*

111. The Board has concluded that there is no substance in the criticism that, in determining the offer price, the Executive did not obtain objective guidance from an independent expert on the assessment of the value of Sky shares.

112. It was contended that such an independent expert assessment would be an objective yardstick against which to test and assess the value attributed by Disney to Fox's stake in Sky and ensure that shareholders in Sky are treated fairly in accordance with the Code. It was submitted that the Panel had not done all that it should have done to ensure that the offer price was fair and reasonable to shareholders in Sky.
113. Elliott took this point without producing to the Executive, the Hearings Committee or the Board any supporting evidence from an expert and without identifying anyone who might qualify as such an expert or indicating what guidance an expert might give to the Executive in this case.
114. Further, as already explained, the determination of the Chain Principle Offer price is not a question of ascertaining a "fair", "true" or "reasonable" value. There is no "fair" value of the Sky shares for an independent expert to determine or give guidance on. The applicable principles of equivalent treatment and shareholder protection in General Principle 1 look to assessing and setting a price by reference to the price paid by Disney for Fox's 39% stake in Sky rather than to questions of "fair", "true" or "reasonable" value as factors in considering the treatment and protection of shareholders. Those concepts are not express or implied requirements of the relevant provisions of the Code. The reference to independent valuation in Note 1 on Rule 9.5, relied on by Elliott, relates to the valuation of consideration other than cash, and is of no assistance.
115. Moreover, the Executive is independent, expert and qualified by relevant experience to deal with the particular problems of setting a Chain Principle Offer price.
116. For those reasons the Board confirms the ruling of the Hearings Committee.

**Rt Hon Lord Collins of Mapesbury, LLD, FBA**

**Rt Hon Sir John Mummery, DL**

**Giles Henderson, CBE**

**John Nelson, CBE, DL**

**Robert Swannell, CBE**

**29 August 2018**

**ANNEX**  
**DECISION OF THE HEARINGS COMMITTEE**

THE TAKEOVER PANEL  
**HEARINGS COMMITTEE (“THE COMMITTEE”)**  
**THE WALT DISNEY COMPANY (“DISNEY”)**  
**SKY PLC (“SKY”)**

**DETERMINATION OF DISNEY’S CHAIN PRINCIPLE OFFER PRICE**

**INTRODUCTION - THE ISSUE**

1. On 27 July 2018, the terms for Disney’s acquisition of Twenty-First Century Fox Inc. (“Fox”) were approved by the shareholders of both companies. The acquisition is to be effected by a merger after a spin-off of certain of Fox’s assets into a new company to be owned by existing Fox shareholders. Fox currently owns about 39% of the ordinary shares of Sky, a stake which, under the City Code on Takeovers and Mergers (“the Code”), is treated as a controlling interest.
2. The issue before the Committee is the price at which Disney should be required to make an offer to the holders of ordinary shares in Sky following completion of Disney’s acquisition of Fox. In that event, an obligation on Disney to make such an offer would arise under the “chain principle” set out in Note 8 on Rule 9.1 of the Code, having regard to a previous ruling of the Executive of the Takeover Panel (“the Executive”) that securing control of Sky might reasonably be considered to be a significant purpose of Disney in acquiring Fox.
3. On 13 July 2018, the Executive ruled that, within 28 days of its acquisition of Fox, Disney’s offer for each ordinary share of Sky (“the Chain Principle Offer”) should be at the price of £14.00 per share unless by then either Fox had acquired 100% of the ordinary shares of Sky, or Comcast Corporation (“Comcast”) or any other third party had acquired more than 50% of the ordinary shares of Sky. The reference to Comcast and its role in the matter are explained below.
4. Following publication of the Executive’s ruling, the Independent Committee of Sky and several of its larger shareholders asked for the Committee to be convened to review the Executive’s determination of the Chain Principle Offer price and the methodology applied to arrive at it. In addition, while not seeking to challenge the Chain Principle Offer price as such, Disney and Fox are critical of the methodology used by the Executive to determine the offer price and have filed submissions and participated in the hearing as interested parties.

## **THE PARTIES**

5. A list of the parties and their advisers is set out in Appendix 1. The parties' respective positions and the submissions they advanced are summarised below.

## **THE COMMITTEE**

6. A list of the members of the Committee who heard this case is set out in Appendix 2.

## **BACKGROUND**

7. On 15 December 2016, Fox announced a recommended cash offer for all the remaining shares of Sky at a price of £10.75 per share. That offer was to be implemented by a scheme of arrangement and was subject to a number of pre-conditions, including certain regulatory clearances which have now been satisfied or waived. At the time of the announcement, the price of £10.75 per share represented a premium of some 36% to the share price of Sky for 9 December 2016, the day before the offer period commenced.
8. On 14 December 2017, Disney and Fox announced a definitive agreement for Disney to acquire Fox. That agreement provided for certain Fox assets to be spun-off into a new company owned by existing Fox shareholders. According to Disney's investor presentation, the consideration payable implied a value of approximately \$28.00 for each share of Fox.
9. Later on 14 December 2017, the Executive announced that it would in due course decide whether Disney's acquisition of Fox (and with it Fox's 39% stake in Sky) would trigger an obligation on Disney to make a mandatory offer for the remaining shares of Sky, something which Disney had disputed.
10. On 27 February 2018, Comcast announced that it was considering making an offer for Sky.
11. By Panel Statement 2018/4 issued on 12 April 2018, the Executive announced that it had informed Disney, Fox and Sky that, within 28 days of completion of its acquisition of Fox, Disney would be required to make a mandatory offer to the holders of ordinary shares in Sky pursuant to Note 8 on Rule 9.1 of the Code. That obligation, it was said, arose as a result of the Executive's finding that securing control of Sky might reasonably be considered to be a significant purpose of Disney in acquiring control of Fox. By this ruling, the Executive also stated that the mandatory offer must be at £10.75 in cash for each ordinary share in Sky, that being the price attributed by Disney to Fox's stake in Sky in the consideration payable by Disney for Fox. The statement went on to provide, however, that Disney would not be obliged to make a Chain Principle Offer if, by the due time for making it, Fox had acquired 100% of the ordinary shares of Sky or Comcast or any other third party had acquired more than 50% of the ordinary shares of Sky.
12. On 25 April 2018, Comcast announced a firm intention to make an offer for Sky under Rule 2.7 of the Code at a price of £12.50 per Sky share. That offer was stated to be conditional upon certain regulatory clearances which have since been received. It

was also subject to 50% acceptance. On the same day, the independent directors of Sky announced that, in light of Comcast's stated intention to make a higher cash offer, they were withdrawing their recommendation of Fox's offer of 15 December 2016.

13. On 13 June 2018, Comcast published a proposal to acquire Fox on the same basis as Disney but at a higher price of \$35.00 in cash for each Fox share. Thereafter, until 19 July 2018 when Comcast publicly withdrew its interest in acquiring Fox, the contest between Fox and Comcast for Sky took place against the backdrop of a battle between Disney and Comcast for control of Fox.
14. Comcast's intervention was followed by an announcement from Disney on 20 June 2018 that it had entered into a revised acquisition agreement with Fox under which its offer price increased to approximately \$38.00 per Fox share. This was subject to a collar arrangement which determined the rate at which Disney shares<sup>1</sup> would be exchangeable for shares of Fox by reference to a specified range for the trading price of Disney shares at completion. Fox shareholders were also given the option of electing for cash or stock subject to 50/50 pro-rating.
15. Disney's revised acquisition agreement with Fox led the Executive to publish Panel Statement 2018/7 on 28 June 2018. By that statement, the Executive announced that it had received conflicting views regarding the impact of the increased price of Disney's acquisition of Fox on the Chain Principle Offer price of £10.75 set by the Executive's ruling of 12 April 2018. The Executive went on to say that it would make a further announcement in due course.
16. On 11 July 2018, Fox and Sky announced an increased recommended cash offer for Sky of £14.00 per ordinary share, to be implemented by a scheme of arrangement. In that offer announcement, it was said that Disney had provided its consent to the increase in debt that Fox would incur as a result of the increased offer. There would, of course, be indebtedness that Disney would take on if and when it completed its acquisition of Fox. The announcement also stated that if Disney's acquisition of Fox did not complete due to a failure to obtain regulatory approvals or in certain other limited circumstances, Disney would reimburse Fox the difference between the consideration of £14.00 per share in Sky payable under the Fox recommended offer and £13.00 for each such share. Disney would also pay any interest and fees on such amount.
17. Comcast's response was swift: later on 11 July 2018 it announced an increased recommended offer of £14.75 for each Sky share. Its offer document was published on 13 July 2018.
18. This was the background to the Executive's ruling of 13 July 2018 in which, as explained above, it announced that, as a result of the increase in the consideration payable under the terms of Disney's acquisition of Fox (announced on 20 June 2018), the Chain Principle Offer price would be increased to £14.00 for each ordinary share of Sky. In that statement (Panel Statement 2018/7) the Executive went on to explain that it had determined the Chain Principle Offer price by analysing, among other matters, the relative contribution of Fox's stake in Sky in the valuation work carried

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<sup>1</sup> That is shares in the new Disney company to be formed for the merger.

out by Disney's financial advisers to support the revised fairness opinion prepared for Disney in June 2018. The Executive also said that it took into account Fox's offer of £14.00 per share announced two days earlier.

19. On 27 July 2018, as previously noted, the terms of Disney's acquisition of Fox were agreed by the shareholders of both companies.

## **RELEVANT PROVISIONS OF THE CODE**

20. Consideration of the Chain Principle Offer price requires an understanding of Rule 9 of the Code and its rationale.

21. The Code is founded on six General Principles each of which reflects a principle set out in the EU Directive on Takeovers 2004/25/EC. General Principle 1 states:

*“All holders of the securities of an offeree company of the same class must be afforded equivalent treatment; moreover, if a person acquires control of a company, the other holders of securities must be protected.”*

22. The Code treats a stake carrying 30% or more of the voting rights as a controlling interest and gives effect to General Principle 1 by requiring a person who acquires such an interest, whether alone or acting in concert with others, to make an offer to other shareholders to purchase their shares. Rule 9.1 of the Code states:

“Except with the consent of the Panel, when:

- (a) any person acquires, whether by a series of transactions over a period of time or not, an interest in shares which (taken together with shares in which persons acting in concert with him are interested) carry 30% or more of the voting rights of a company; or
- (b) any person, together with persons acting in concert with him, is interested in shares which in the aggregate carry not less than 30% of the voting rights of a company but does not hold shares carrying more than 50% of such voting rights and such person, or any person acting in concert with him, acquires an interest in any other shares which increases the percentage of shares carrying voting rights in which he is interested,

such person shall extend offers, on the basis set out in Rules 9.3, 9.4 and 9.5, to the holders of any class of equity share capital whether voting or non-voting and also to the holders of any class of transferable securities carrying voting rights. Offers for different classes of equity share capital must be comparable; the Panel should be consulted in advance in such cases.”

23. The price at which an obligatory Rule 9 offer is to be made by a party acquiring a stake of 30% or more is regulated by Rule 9.5. Rule 9.5 states:

- (a) “An offer made under Rule 9 must, in respect of each class of share capital involved, be in cash or accompanied by a cash alternative at not less than the highest price paid by the offeror or any person acting in concert with it for any interest in shares of that class during the 12 months prior to the announcement

of that offer. The Panel should be consulted where there is more than one class of share capital involved.

- (b) If, after an announcement of an offer made under Rule 9 for a class of share capital and before the offer closes for acceptance, the offeror or any person acting in concert with it acquires any interest in shares of that class at above the offer price, it shall increase its offer for that class to not less than the highest price paid for the interest in shares so acquired.”

- 24. Accordingly, where a person acquires control of a company, Rule 9 of the Code provides the opportunity for other shareholders to exit by selling their shares to the party with control at the highest price paid by that party (or by those acting in concert with it) during the twelve months prior to the making of the obligatory offer. Furthermore, if after the announcement of the Rule 9 offer but before it closes for acceptance, the offeror or any person acting in concert with it acquires additional shares at a higher price, shareholders of the relevant class are entitled to the benefit of an offer at that higher price.
- 25. By this means, where a party acquires a controlling stake in a company Rule 9 of the Code enables other shareholders to sell their shares at whatever premium price was paid to obtain control of the company. It is important to note, however, that the obligatory offer price reflects the highest price actually paid to gain control of the company (or to consolidate or secure control when additional shares are acquired by a party which already holds a stake of at least 30% but not more than 50%): it does not involve an obligation to offer a fair or reasonable price or a price which best reflects the true value of the company.
- 26. It is in this context that one has to read the “chain principle” set out in Note 8 on Rule 9.1. Note 8 states that:

“Occasionally, a person or group of persons acting in concert acquiring shares resulting in a holding of over 50% of the voting rights of a company (which need not be a company to which the Code applies) will thereby acquire or consolidate control, as defined in the Code, of a second company because the first company itself is interested, either directly or indirectly through intermediate companies, in a controlling block of shares in the second company, or is interested in shares which, when aggregated with those which the person or group is already interested in, secure or consolidate control of the second company. The Panel will not normally require an offer to be made under this Rule in these circumstances unless either:

- (a) the interest in shares which the first company has in the second company is significant in relation to the first company. In assessing this, the Panel will take into account a number of factors including, as appropriate, the assets, profits and market values of the respective companies. Relative values of 50% or more will normally be regarded as significant; or
- (b) securing control of the second company might reasonably be considered to be a significant purpose of acquiring control of the first company.”

- 27. Thus, where Company A acquires shares carrying over 50% of the voting rights of Company B and, as a result, obtains or consolidates a controlling stake in Company C,

Company A will not be required to make a Rule 9 offer to shareholders of Company C unless one or both of two stated conditions applies. In this case, the triggering condition is that securing control of Company C (Sky) might reasonably be considered to be a significant purpose of Company A's (Disney's) acquisition of Company B (Fox).

28. The Code does not stipulate how the price of an offer made pursuant to the "chain principle" is to be calculated. Rule 9.5 of the Code has no direct application in this case because neither Disney nor any person acting in concert with it has purchased shares in Sky during any period relevant for the purposes of the Code. Furthermore, typically in transactions such as this the price attributable to Company A's acquisition of Company B's stake in C is not identified in the consideration payable by A for the assets of B.
29. It appears from the Executive's written submission in this case to the Committee that, in October 2008, the Takeover Panel Code Committee considered whether it should propose in a public consultation document that Note 8 on Rule 9.1 be amended to stipulate a method for calculating a chain principle offer price. The proposal under consideration was that the offer for Company C should normally be made at the same percentage premium or discount to the quoted price of the shares of Company B as had been paid by the acquirer (Company A) for the shares in Company B, unless this produced a manifestly unfair result. Under that approach, therefore, whatever percentage premium to the quoted price had been paid by A for the shares of B would be the premium price to be offered by A to the other shareholders of C. The Code Committee decided, however, that such an approach would be too simplistic and would in many cases be inappropriate, for example where Company B and Company C were valued on different bases. Accordingly, the Code Committee concluded that the Takeover Panel's policy on setting a chain principle offer price should be developed on a case by case basis without amending the Code.
30. It also appears from the Executive's written submission that, over the course of the last thirty years, there have been five cases in which an offer has been required under the "chain principle". In each case, however, the parties involved reached agreement on the offer price. Furthermore, no such case involved the distinguishing features of the present case, in which:
  - (i) Company B (Fox) has substantial assets other than its stake in Company C (Sky);
  - (ii) Company B (Fox) will spin-off a portion of its assets before Company A (Disney) completes its acquisition;
  - (iii) Company C (Sky) is itself the subject of competing offers from Company B (Fox) and Comcast; and of most significance
  - (iv) Company B's (Fox's) current offer for Company C (Sky) was announced shortly after Company A's (Disney's) revised agreement to acquire Company B (Fox) and was made with Company A's approval and support.
31. This last feature is particularly significant because it justifies viewing Fox's current offer for Sky, if not as a proxy offer by Disney, then at least as an offer made at a price that indicated the value attributed by Disney to consolidating control of Sky in the context of Comcast's competing offer of £12.50 per ordinary share. A central

issue at the hearing before the Committee was the relevance, if any, of Fox's 11 July 2018 bid for the remaining shares of Sky to the value attributed by Disney to Fox's 39% interest in Fox in the consideration payable for acquiring the assets of Fox. As previously noted, the revised, increased consideration for Disney's acquisition of Fox had been announced three weeks earlier on 20 June 2018.

32. In circumstances where the Code does not regulate the process of determining a Chain Principle Offer price and previous rulings of the Committee and Takeover Appeal Board afford no precedent, the Committee must, in its view, attempt to identify the approach which, on the particular facts of this case, best reflects the rationale of Rule 9. That will involve identifying an approach which gives effect to the principle that where a party acquires control of a company or (if already the holder of shares controlling at least 30% but no more than 50% of the voting rights) consolidates or secures control, the other shareholders should be offered the highest price actually paid by that party in obtaining or securing control. By this mechanism the Code seeks to ensure equivalent treatment for shareholders.

### **THE EXECUTIVE'S APPROACH TO DETERMINING THE CHAIN PRINCIPLE OFFER PRICE**

33. The Executive submits that in determining a Chain Principle Offer price it sought first to determine what proportion of the consideration payable by Disney under its agreement to acquire Fox was attributable to Fox's 39% shareholding in Sky.
34. This involved an objective analysis of relevant materials directed, not to establishing the relative intrinsic value of the stake in Sky to the other assets of Fox, but to establishing what proportion of the purchase consideration Disney attributed to acquiring Fox's stake in Sky. This involves inferring from the relevant material the proportion of the total consideration payable for Fox's assets to be received by its shareholders for their 39% interest in Sky. Having established the proportion of the consideration attributable to Fox's stake in Sky, it becomes possible to calculate a Chain Principle Offer price per share.
35. In this case the Executive has determined a Chain Principle Offer price on two occasions, once in light of the consideration payable under the initial agreement for Disney to acquire Fox announced on 14 December 2017 ("the Initial Acquisition Agreement") and again in light of the increased consideration payable under the revised acquisition agreement announced on 20 June 2018 ("the Revised Acquisition Agreement"). Although the original Chain Principle Offer price set by Panel Statement 2018/4 has now been superseded, it remains relevant to consider how it was arrived at for two reasons:
  - (1) the Independent Committee of Sky and the Sky Shareholders Group represented by Greenhill maintain that the adjusted Chain Principle Offer price should be determined by increasing the original price of £10.75 per share by the same percentage as the total consideration originally payable for the assets of Fox was increased under the Revised Acquisition Agreement. Both Disney and Fox objected to this so called "linear approach" for various reasons, including that the price per Sky share actually attributed by Disney to Fox's

39% interest in Sky under the Initial Acquisition Agreement was, Disney maintains, substantially less than £10.75; and

- (2) Fox maintained that the Executive, in adjusting the Chain Principle Offer price to £14.00 per share, was obliged to follow the same methodology as it had adopted in determining the original price of £10.75, but failed to do so.

Accordingly, it becomes necessary to describe how the Executive arrived at its original Chain Principle Offer price and whether it subsequently adopted an inconsistent approach in adjusting it. It also becomes relevant to ask whether the figure of £10.75 is an appropriate basis for extrapolating to a revised Chain Principle Offer price.

36. The Executive describes the steps it took to establish the proportion of the consideration payable for the Fox assets that were attributable to Fox's stake in Sky as:
  - (1) making enquiries of Fox and Disney in order to determine whether in negotiating the purchase of Fox, any price per share was attributed to Fox's shareholding in Sky;
  - (2) examining whether there is other evidence which indicates an agreement between Disney and Fox on a price per share for Fox's shareholding in Sky; and
  - (3) examining the valuation materials that were prepared to support Disney's offer for Fox in order to ascertain whether any prices derived from the previous two steps were in line with the contribution of the Sky stake to the valuation of the assets of Fox that Disney was to acquire.
37. As stated in Panel Statement 2018/4, step 3 was undertaken in order to validate the assertion by Disney and Fox that £10.75 was the value per ordinary share of Sky that they actually attributed to the stake in Sky during the merger negotiations. According to the Executive, while any price attributed by the negotiating parties to the stake in Sky is relevant and provides a useful starting point, it would have to be tested against other material (particularly the valuation work for the transaction carried out by and on behalf of Disney) in order to determine whether any attribution of price for the stake in Sky was reasonable in light of the overall valuation of Fox's assets. Without such a cross-check, it would be open to parties to any transaction which might potentially trigger an obligation to make a Chain Principle Offer, to ascribe an artificially low value to Company B's interest in Company C in order to accommodate Company A (the acquirer of Company B).

## **THE ORIGINAL CHAIN PRINCIPLE OFFER PRICE**

38. As a first step in the process of determining the original Chain Principle Offer price, the Executive approached Disney and Fox to establish whether any value had been attributed to the stake in Sky during negotiations for the Initial Acquisition Agreement. Fox claimed that at an early stage in negotiations they had made it clear that the price for the stake in Sky was £10.75 per share and that thereafter price negotiations had centred on Fox's other assets. Fox also claimed that Goldman Sachs,

its advisers, had attributed a value of £10.75 per share in materials provided to the Fox board. Disney's position was more nuanced: it claimed that the focus of the negotiations was directed to agreeing an overall price for the Fox assets but that its own valuation of Fox's interest in Sky was less than £9.00 per share. Disney also disclosed, however, that a value of £10.75 per Sky share had been included in its presentation to investors accompanying the announcement as that was the current value of the Fox offer for Sky and so constituted a verifiable external valuation of the asset. Accordingly, there was evidence that both parties to the transaction had attributed a value of £10.75 per ordinary share to Fox's 39% stake in Sky.

39. The Executive then examined the valuation materials prepared both by and on behalf of Disney to see whether they afforded support for this price. Disney had received a fairness opinion from JP Morgan and Guggenheim & Partners and the Executive examined a copy of the projections supporting that opinion. Those projections had been published when Disney filed with the SEC its Form S-4 and other documents in connection with the proposed shareholder meetings of Disney and Fox.
40. The Executive then focussed on a particular discounted cash flow analysis ("DCF") directed to valuing Fox's assets on the hypothesis that its offer for the remaining shares of Sky did not proceed to completion (a scenario that reflected Fox's current ownership of a stake of 39%). A summary of that analysis was subsequently published in Disney's Form S-4, filed on 18 April 2018. Although Disney's advisers had also prepared valuations based on multiples of EBITDA paid on comparable transactions, it was felt that a DCF analysis was the most appropriate valuation tool in the circumstances and, although dependent on multiple assumptions, was better able to capture the long-term and evolving value of an asset than a valuation based on a multiple of a single year's EBITDA. It appeared to the Executive that a DCF based valuation would also have the advantage of having been built up from sub-analyses of the various constituent parts of Fox's assets.
41. The Executive made it clear that it wished to understand what proportion of the whole DCF valuation was represented by Fox's 39% stake in Sky. In response, Disney's advisers presented three different valuation ranges:
  - (a) a standalone DCF in which the value projected disregarded the impact of any synergies that would be gained under Disney's ownership;
  - (b) a standalone DCF to which was added the value of cost synergies that Disney expected after the acquisition; and
  - (c) as in (b), but also bringing into account the revenue synergies that Disney expected.

Because Disney took the view that no synergies could be gained from 39% ownership of a publicly listed company, bringing into account anticipated synergies added value to Fox's other assets and thereby operated to increase the value of those other assets relative to the value of its stake in Sky. Accordingly, the percentage contribution to the DCF valuations represented by the advisers' DCF valuations of Fox's stake in Sky was highest on a standalone basis and lowest on a basis that brought into account both cost and revenue synergies. Disney's case is that the prospect of cost and revenue synergies is a driving motive in its acquisition of Fox but that all the anticipated synergies are referable to the integration of Fox's US assets with its business.

42. The Executive's approach was to take a mid-point valuation on the basis that the prospect of deriving synergies almost always has some impact on the acquisition price. According to the Executive, it is rare for buyers to acquire companies without intending to derive any synergies and rare, therefore, to be able to acquire a company without paying a premium. Equally, it is rare for a buyer to pay the full value of both cost and revenue synergies over to a seller. In the event, the Executive opted for that DCF valuation which brought into account cost synergies only; this was taken by the Executive as a rough proxy for the mid-point between a standalone valuation and a valuation that brought into account both cost and revenue synergies.
43. That "mid-point" projection prepared by Disney's bankers indicated that the stake in Sky represented 18% of the DCF valuation of all Fox's relevant assets. Applying that percentage to the total consideration payable under the Initial Acquisition Agreement and dividing the result by the number of Fox's shares in Sky, produced a price per share of £10.53. The calculation, therefore, produced a number lower than that which Disney accepted and Fox maintained had been formally attributed to Fox's stake in Sky out of the consideration payable.
44. Disney had prepared its own projections of relative value but, apart from the standalone valuation, these produced figures significantly lower than £10.75 per share. In addition, the Committee was told by Disney at the hearing that, at a presentation by management to the board, it had produced a DCF valuation of its own of Fox's stake in Sky at about £8.80 per share. This was an "absolute" value as distinct from an exercise to establish the relative values of the stake in Sky and Fox's other assets. In the event, the Executive selected £10.75 per share as the price publicly attributed by Disney to acquiring Fox's interest in Sky, having established that the value projections prepared by and on behalf of Disney did not exceed this figure. This ruling was accepted by Disney, Fox and the Independent Committee of Sky.
45. The Committee notes in passing that on 28 June 2018, Elliott Advisors (UK) Limited ("Elliott"), a substantial shareholder in Sky, requested that the Committee be convened to review the ruling of 12 April 2018. That request was dismissed by the Chairman of the Committee on the ground that it had been made well after expiry of the time allowed under the Committee's Rules of Procedure and convening the Committee would serve no useful purpose having regard to the Executive's statement of 28 June 2018 that it intended to reconsider the Chain Principle Offer price in light of the Revised Acquisition Agreement. Elliott lodged an appeal to the Takeover Appeal Board against the Chairman's ruling but has since withdrawn the appeal.

#### **THE ADJUSTED CHAIN PRINCIPLE OFFER PRICE**

46. By the time the Executive came to review the Chain Principle Offer price in light of the increased consideration payable under the Revised Acquisition Agreement, circumstances had changed.
47. On 25 April 2018, Comcast had announced a firm intention to make an offer for Sky at a price of £12.50 per ordinary share, an offer which was recommended by the Independent Committee of Sky until competing increased offers by Fox and Comcast were made on 11 July 2018. By the time the Executive came to review the Chain

Principle Offer price, the evidence strongly suggested that, in light of the competitive threat, Disney was intent on acquiring 100% of Sky if it could. Disney had, for example, assisted Fox in acquiring regulatory approval from the UK government by undertaking to acquire assets which the regulator and government wanted spun-off by Fox to preserve media plurality. Indeed, it was conceded on behalf of Disney at the hearing that it is Disney's intention to acquire 100% of Sky if it can do so at a price that makes sense. This raised the question whether, in determining the value that Disney attributed to the 39% stake in Sky (i.e. the amount the shareholders of Fox were actually to receive for their interest in Sky under the Revised Acquisition Agreement) the value of the 39% interest as a springboard for obtaining 100% ownership and thereby obtaining practical control ought to be taken into account.

48. Furthermore, in contrast to the position under the Initial Acquisition Agreement, Disney had not publicly attributed a price per share to Fox's stake in Sky in investor presentation material. Against this, shortly after announcing the Revised Acquisition Agreement, Disney had effectively sponsored a bid by Fox for the remaining shares of Sky at £14.00 per share. In its written submission to the Committee, the Executive maintained that this was "compelling evidence of an agreed attribution of value by Disney". In its oral submissions the Executive described this as a "data point" against which to compare the valuation material prepared by and for Disney and stood by its position that this was compelling evidence of Disney's attribution of value to the stake in Sky made some three weeks earlier under the Revised Acquisition Agreement.
49. Having heard the Executive, the Committee accepts that this was, in summary, the process which it followed in adjusting the Chain Principle Offer price in light of the increased consideration payable under the Revised Acquisition Agreement. Whether that methodology was right or wrong, we do not believe that it was inconsistent with the approach adopted previously. On both occasions the Executive attempted to identify the price which the shareholders of Fox would actually receive for their interest in Sky prior to directing that the same price be offered by Disney to Sky's other shareholders. The price actually received by Fox's shareholders for Fox's stake in Sky will, of course, be the same as the price actually attributed by Disney to that particular asset of Fox.
50. But the circumstances had changed since the first assessment of the Chain Principle Offer price, as had the material available to identify the relevant attribution. Whereas under the Initial Acquisition Agreement the Executive had evidence of a published attribution of value which was agreed by both parties to the transaction and which remained valid when compared to the valuation material prepared by or on behalf of Disney, on the second occasion there was no such starting point. In contrast, on the second occasion the increase in consideration payable under the Revised Acquisition Agreement was followed shortly thereafter by an increased bid by Fox for the remaining shares of Sky. This was a bid which Disney had authorised and supported which appears to have indicated to the Executive that Disney's increased consideration under the Revised Acquisition Agreement took into account the value of the 39% stake in Fox as a springboard for consolidating control of Sky in light of the competitive threat posed by Comcast's then recommended offer of £12.50. In other words, for the Executive, the Fox offer price of 11 July 2018 was a "data point" which could be applied retrospectively to shed light on the attribution of value made by Disney under the Revised Acquisition Agreement announced on 20 June 2018.

51. The Executive then asked itself whether £14.00 for each ordinary share of Sky was a value supported by the valuation materials as being consistent with the proportional contribution of the Sky stake to the other assets of Fox passing under the Revised Acquisition Agreement. Essentially, as before, these were DCF projections of the relative value of the stake in Sky and the other assets of Fox, that is to say, they estimated the percentage of all the assets of Fox passing under the Revised Acquisition Agreement to the new merged company constituted by the equity value of the stake in Sky. Disney's internal valuations of relative value produced a price per share for Sky of £12.71 or £10.18 depending upon whether only the cost synergies to be expected from the acquisition are taken into account or both anticipated cost and revenue synergies are included in value. The equivalent valuations produced for the Executive by Disney's advisers produced corresponding figures of £14.85 and £11.65 per ordinary share.
52. In considering whether these projections were consistent with an offer price of £14.00 per share, the Executive took into account the strong representations made by Disney that the synergies expected from the merger with Fox all flowed from Fox's US assets and, specifically, from the advantages of integrating those assets with Disney's. Having regard to this, the Executive concluded that some weight should be attributed to revenue as well as costs synergies in the relative valuations of the stake in Sky to Fox's other assets. This suggested that a Chain Principle Offer price of £14.00 per share was generous when tested against the valuation exercises available: at any rate, it was certainly not too low.
53. Accordingly, by Panel Statement 2018/7 of 2018 the Executive announced that the Chain Principle Offer price should be £14.00 for each ordinary share of Sky. Before doing so, it considered conflicting arguments from the interested parties broadly similar to those advanced before the Committee at the hearing.

#### **THE PARTIES' POSITIONS IN SUMMARY**

54. What follows is only a brief summary of the arguments advanced before the Committee at the hearing and in written submissions served previously. These arguments were advanced forcefully and with clarity: the Committee has considered each of them carefully and in detail, albeit only a brief summary may be reproduced here if an already lengthy ruling is not to be even longer.

## DISNEY'S CASE

55. Disney accepted both the original and revised Chain Principle Offer prices for reasons described as “pragmatic” while maintaining that the Executive had erred in considering anything other than Disney’s own valuations of Fox’s 39% stake in Sky. Had the Executive focussed solely on the value that Disney had attributed to the stake in Sky, both the original and adjusted Chain Principle Offer prices would have been lower. The Committee was told by Mr Warbrooke, the Disney employee who led Disney’s internal valuation work both for the Fox assets overall and the stake in Sky specifically, that prior to the Initial Acquisition Agreement and the Revised Acquisition Agreement, Disney had prepared DCF projections which valued the 39% stake in Sky at about £8.80 and £11.80 per share respectively. These, we were told, were the valuations provided to the Disney board in the context of the board’s consideration of the Initial and Revised Acquisition Agreements.
56. Disney maintained that it was wrong to place reliance on projections prepared by Disney’s advisers for the purpose of fairness opinions as the purpose of such opinions was not to value the proposed acquisition but to give the board comfort that their own valuations were within a range considered reasonable. Moreover, Disney did not rely upon the fairness opinions in reaching its own estimates of value. Disney accepted that its investor presentation for the Initial Acquisition Agreement attributed a value of £10.75 per share to the stake in Sky but said that this merely recognised that investors tend to need a market guidepost for making their own calculations and £10.75 was at the time the only live bid for the shares in Sky not already owned by Fox. Similarly, although there was no further investor presentation for the Revised Acquisition Agreement, £12.50 per share (being the price offered by Comcast which at the time had been recommended by the Sky Independent Committee) was the value attributed by Disney in material put before the board to enable the board to take a view on the increased consideration payable. Disney maintained, moreover, that a price of £12.50 reflected the improvement in the Sky asset since the previous valuation, an improvement largely attributable to Sky’s achievement in renewing English Premier League broadcasting rights at a lower price than expected.
57. Central to Disney’s case was the contention that deriving cost and revenue synergies was a core motive for the acquisition of Fox but that all such synergies were to be derived from integrating Fox’s US assets. According to Disney, absolutely no synergies could be attributed to its ownership of a 39% stake in Sky. A 39% stake in a publicly quoted company is treated as a controlling interest by the Code, but it does not impart the practical control that allows a business to be restructured and integrated with that of the party owning such a stake. Disney admittedly wished to acquire 100% of Sky if it could do so at a price which it considered reasonable, but that should not (and as Disney told the Committee, did not) affect the value attributed to Fox’s 39% stake in Sky.
58. Why then did Disney accept both the original and adjusted Chain Principle Offer prices if they were so much higher than Disney’s internal valuations? The answer as regards the initial Chain Principle Offer price is summarised above. As regards the revised Chain Principle Offer price of £14.00 per share, the answer appears to be that it was thought advisable or appropriate to accept it given that it reflected the price just offered by Fox with Disney’s authority and support. It is important to note, therefore,

that on both occasions Disney has, for whatever reason, accepted as a Chain Principle Offer price, the price of an outstanding offer by Fox for the 61% of shares in Sky that it does not currently own. It did this while maintaining that in determining the Chain Principle Offer price it was permissible to value only the 39% interest in Sky without taking into account the advantage such an interest provided in bidding for 100% ownership (or indeed the potentially enhanced value of a 39% stake when someone else was also bidding for control).

## FOX

59. Fox's position was largely aligned with that of Disney. As regards the initial Chain Principle Offer price, it maintained that £10.75 was the price for Fox's interest in Sky agreed by both parties to the merger of Fox with Disney. As such, that price had been properly taken as the value attributed by Disney to Fox's interest in Sky, the correct approach to determining a Chain Principle Offer price being to identify the value actually attributed by Company A to Company B's stake in Company C.
60. Fox also referred to the Executive's statement in Panel Statement 2018/4 that "in the circumstances of this case, the Executive has determined that the Offer should be at the price per share attributed by Disney to Fox's shareholding of approximately 39% of the ordinary shares in Sky in connection with the Acquisition...". Fox maintains that in light of this statement it would be unlawful for the Executive to adopt any different approach to any later assessment in the same case of a Chain Principle Offer price. We have already explained that, on the facts as the Committee sees them, this argument goes nowhere. In its second determination of a Chain Principle Offer price the Executive once again attempted to identify the price per share actually attributed by Disney to Fox's stake in Sky, but in this instance the circumstances were materially different. There was no evidence of an agreed attribution by the parties in the acquisition of Fox to the stake in Sky or even evidence of such an attribution by Disney alone. There was, however, a recent bid by Fox which Disney had sponsored and which, according to the Executive, provided some evidence of the value that Disney had attributed to the stake in Sky when increasing the consideration payable under the Revised Acquisition Agreement. This was the "data point" which the Executive took as a starting point and which it then tested against valuation material of the sort to which it had referred in its previous determination of the Chain Principle Offer price.
61. As regards the revised Chain Principle Offer price, Fox's case was that as both Disney and Fox had valued the stake in Sky at £12.50 per share in papers prepared by management for their respective boards, that was the price which the Executive should have taken as the revised Chain Principle Offer price.
62. Like Disney, however, Fox has accepted the price of £14.00 per share. The reason given in its written submissions to the Committee was that the 11 July 2018 bid at £14.00 per share "...could be said to provide evidence of Disney's willingness to attribute a value of £14.00 to Sky's shares in order to secure control of Sky." This echoed an observation made elsewhere in Fox's written submissions that the "increased offer of £14.00 could therefore be said to be an indicator of the value attributed by Disney to Sky shares". Fox went on to note, however, that the offer of

£14.00 which Disney had authorised and supported was only made after the terms of the Revised Acquisition Agreement had been agreed.

## **THE INDEPENDENT COMMITTEE OF SKY**

63. The Independent Committee contended for a Chain Principle Offer price of £14.59 for each ordinary share of Sky. This figure was arrived at by applying a version of the so-called linear approach referred to previously. The consideration under the Initial Acquisition Agreement was payable in Disney shares, with the result that the value per share received by Fox's shareholders would depend on the agreed ratio of Fox to Disney shares. The \$28.00 valuation for each ordinary share in Fox under the Initial Acquisition Agreement was apparently derived from a volume weighted average price of Disney's shares over the 30 days preceding the date on which the share exchange ratio under the Initial Acquisition Agreement was agreed. In contrast, the \$38.00 per share value derived from the consideration payable under the Revised Acquisition Agreement, came with an option to receive the consideration in cash or stock in the new Disney corporation, subject to 50/50 pro-rating. Under the revised Acquisition Agreement, the ratio of Fox to Disney shares varied within a fixed range depending on the average Disney share price at completion<sup>2</sup>.
64. The Independent Committee contended that the revised Chain Principle Offer price should be arrived at by increasing the original Chain Principle Offer price by 35.7%, that being the percentage increase by which the cash value of the consideration payable for all the relevant assets of Fox increased from the Initial to the Revised Acquisition Agreements. This exercise would produce an adjusted Chain Principle Offer price of £14.59 for each ordinary share of Sky.
65. The Independent Committee did not suggest that a linear approach of the sort proposed would be a suitable methodology in all cases, but it did maintain that it was the best technique in the current circumstances bearing in mind that, if one had due regard to the performance of Sky during the period between Initial and Revised Acquisition Agreements, it could not be said that the value of the Sky stake relative to Fox's other assets had declined from that implied by the initial Chain Principle Offer price of £10.75. The Committee found the simplicity of this approach attractive, but it did involve the conceptual difficulties described below.
66. The essential thrust of the Independent Committee's case, which the Committee accepted in principle, was that while it may have been legitimate at the time of the Initial Acquisition Agreement to value the 39% stake in Fox in isolation and without reference to its enhanced value to Disney flowing from the prospect of moving from 39% to 100% ownership, it was clear that such an approach was no longer valid by the date of the Revised Acquisition Agreement. By then, Disney had clearly evinced an intention to acquire the strategic benefits of 100% ownership of Sky in the face of a competing bid by Comcast. This meant, according to the Independent Committee, that the amount per share actually received by Fox's shareholders under the Revised Acquisition Agreement would inevitably be enhanced by the strategic possibilities perceived by Disney in using a 39% stake as a springboard for acquiring 100% ownership of Sky. As we previously noted, the Committee accepts this argument in

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<sup>2</sup> The collar arrangement previously referred to.

principle, but the question is whether the linear approach advocated by the Independent Committee is a more effective method of capturing the enhanced value of the 39% stake than using as a start point the offer which Disney had authorised and supported Fox to make for the remaining shares of Sky shortly after the Revised Acquisition Agreement had been announced.

#### **THE SHAREHOLDER GROUP REPRESENTED BY GREENHILL**

67. This Shareholder Group collectively holds interests in securities representing some 9.3% of the total voting rights of Sky. It includes Elliott which is also represented by Mr Michael Todd QC who advanced submissions on Elliott's behalf which in part, but not entirely, adopted the approach of Greenhill.
68. In very broad summary, the Greenhill submission advocated a variant on the linear approach proposed by the Independent Committee along with a series of upward adjustments to the figure produced by that exercise to take account of factors which are said to have a specific bearing on the relative values of the stake in Sky and Fox's other assets. Because it is said that the information and independent opinion necessary to conduct this exercise reliably is not currently available, Greenhill submits that the Committee should not determine a Chain Principle Offer price but should remit the matter to the Executive to determine the matter afresh in accordance with the approach advocated by Greenhill.
69. Greenhill's approach takes as a given the original Chain Principle Offer price of £10.75. As a first step in the exercise it then calculates an increase of 28.7% in the enterprise value implied by Disney's revised consideration for Fox when compared to the corresponding enterprise value implied by the consideration payable under the Initial Acquisition Agreement. The increase in enterprise value is said to convert into an equity value for Sky of £26.2 billion under the Revised Acquisition Agreement, as compared to the corresponding equity value of £18.8 billion implied by the Initial Acquisition Agreement. Those Sky equity values appear to have been arrived at after deducting the same figure for Sky net debt of £7.1 billion, whereas Sky's net debt had apparently increased over the relevant period. Applying to the original Chain Principle Offer price the same uplift as the increase in the calculated Sky equity values, produced a revised Chain Principle Offer price of £15.01 per share.
70. That figure of £15.01 should then be increased to take account of a variety of factors which Greenhill contends would have operated to increase the value per share of Fox's stake in Sky relative to the other assets of Fox acquired under the Revised Acquisition Agreement. These include the positive performance of Sky during the period between the Initial and Revised Acquisition Agreements (in particular the renewal of English Premier League broadcasting rights at an unexpectedly favourable price), the removal of any part of the consideration premium paid to Fox from those assets which Disney is obliged to sell after the acquisition to comply with regulatory requirements, the fact, as alleged by Greenhill, that the market had already priced in the advantages for Fox's business of US tax reform by the date of Disney's first offer and the synergies for Disney in acquiring 100% ownership of Sky.
71. Greenhill maintained that it was not possible to calculate reliably the uplifts to the price of £15.01 per share demanded by these factors; hence the remedy which it

sought of remitting the matter to the Executive with directions for conducting a fresh determination of the Chain Principle Offer price.

## **ELLIOTT'S POSITION**

72. As regards the impact on the value to be attributed to Fox's stake in Sky of the factors relied upon by Greenhill, Mr Todd QC adopted Greenhill's submission. Elliott's position however, differed in two important respects from that of the rest of the Shareholder Group:
- (1) Elliott maintained that the object of the exercise was to determine the true value of Fox's stake in Sky relative to all Fox's relevant assets - and that exercise required the Executive to obtain independent expert opinion to provide the necessary guidance; and
  - (2) Elliott did not accept the original Chain Principle Offer price of £10.75 per share, contending that it would have been substantially higher had a correct approach to the relative valuation of the stake in Sky to all Fox's relevant assets been followed. Accordingly, any extrapolation from an initial Chain Principle Offer price ought to have been from a substantially higher base figure than £10.75.
73. The essential thrust of Elliott's case was that the Executive's approach was too dependent upon material produced by or on behalf of Disney and Fox, both of whom had the same strong interest in valuing on a basis that would minimise the Chain Principle Offer price. Only a determination of the true value of Fox's stake in Sky relative to the totality of Fox's relevant assets could provide fairness to other shareholders in Sky, and that assessment of value could only be made in light of guidance provided by an independent expert opinion.

## **ANALYSIS**

74. Rules 9.1 and 9.5 of the Code give effect to General Principle 1 by requiring a party that acquires a controlling stake in a company to make an offer to other shareholders at the highest price paid by that party (or by those acting in concert with it) during the 12 months preceding the announcement of the offer. Rule 9.1 also imposes an obligation to make such an offer on a party that already holds shares carrying at least 30% and not more than 50% of the voting rights if that party (or persons acting in concert with it) acquires more shares. These Rules have a twin rationale:
- (1) to secure equivalent treatment of the shareholders of the offeree company by ensuring that whatever price has been paid by the acquiring party to obtain or consolidate control (and it would usually be a premium price) would be offered to other shareholders; and
  - (2) to protect the shareholders of the offeree company by giving them the opportunity to realise their shares and exit having regard to the acquiring party's assumption or consolidation of control.

75. In the Committee's view, it is crucial to note that Rule 9 obliges the party in question to offer to other shareholders the highest price actually paid, not a price which represents the true or fair value of the company's shares at a given time.
76. Note 8 on Rule 9.1 extends the mandatory offer obligation to situations in which a party (A) acquires a company (B) which holds a controlling interest in another company (C) if, amongst other things, securing control of C might reasonably be considered to be a significant purpose of A in acquiring B. The wording of Note 8 applies to cases where A consolidates as well as obtains a controlling interest in C through its acquisition of B.
77. As noted above, in the Committee's view, the Chain Principle Offer price payable under Note 8 should give effect as closely as possible to Rule 9 and its rationale and, by so doing, to General Principle 1 which Rule 9 serves to implement. This means that, by extension of the traditional application of Rule 9, a Chain Principle Offer price will attempt to reflect the price actually payable by A for B's controlling interest in C, not some fair or true value of the stake in C assessed at any particular time. The object is to ensure that whatever price was received by the shareholders of B for their shares in C will be offered by A to C's other shareholders, who can then choose whether or not to accept it. Rule 9 is intended to secure equivalent treatment for the shareholders of the offeree; it does not offer some generalised concept of fair treatment. It may be said, however, that by securing equivalent treatment for the shareholders of an offeree and giving them the opportunity to exit at the best price paid by the acquirer to obtain or consolidate control, Rule 9 does ensure that such shareholders are treated fairly.
78. Accordingly the Committee rejects Elliott's submission that the Chain Principle Offer price should reflect the true value of Fox's stake in Sky: in the Committee's view it should reflect the price actually received by Fox's shareholders from Disney for Fox's stake in Sky.
79. Identifying the price actually paid or attributed by A for B's stake in C does not, however, mean that the Executive is bound to accept the price that A, or A and B together, say is attributable to acquiring the stake in C. An approach that accepts self-certification by A of the price attributed to B's interest in C obviously invites abuse. No doubt any representation of A regarding the price payable for the stake in C will be one piece of evidence which the Executive will take into account, but there would normally be good reasons for not accepting A's say so without testing it against other material. As Elliott and the rest of the Shareholder Group have forcefully pointed out, in this case both Disney and Fox shared a common interest in minimising the Chain Principle Offer price, Disney for reasons that are obvious and Fox because part of the consideration would be received in Disney shares the value of which it had an interest in preserving. To recognise this conflict of interest in attributing a value to the stake in Sky is not to doubt the integrity of those involved, but just to acknowledge commercial reality.
80. The Committee accepts, however, that the Executive is experienced in testing the evidence of parties who have an interest in securing a particular outcome, this being the sort of assessment which it carries out routinely. In this case, for example, the Executive did not accept Disney's or Fox's say so; it proceeded to determine

objectively what price was actually attributed by Disney and received by Fox's shareholders for Fox's stake in Sky. Scepticism of this sort does not mean that the valuations produced for the Disney board by management were done other than conscientiously and diligently, simply that the board may be expected to take into account other factors in deciding whether to proceed with and recommend to shareholders a proposed acquisition. In the Committee's view, in this case the principal factors likely to have influenced the board's view of the value of Fox's stake in Sky are twofold. One such factor was Sky's favourable trading performance during the period since the Initial Acquisition Agreement; and the other was the enhanced value of a 39% stake in Sky when Disney was evidently intent upon competing with Comcast for practical control. In such circumstances, Fox's 39% stake had a strategic value in moving to 100% ownership and thereby deriving the synergies which would flow from practical control. It was repeatedly urged upon the Committee at the hearing that the Disney CEO is on record as having recently described Fox's stake in Sky as "the jewel in the crown". Given that Disney insists that no synergies may be derived from 39% ownership of Sky, a description of this nature must connote the value of this stake as a platform for acquiring strategic control.

81. In summary, in the Committee's view, the Executive did approach the determination of the Chain Principle Offer price objectively. The object of the exercise, however, was to infer from the relevant data what price is actually to be paid by Disney and received by Fox's shareholders for Fox's stake in Sky. The material to enable the Executive to infer the price actually paid by A and received by B for its stake in C will obviously vary from case to case, as is borne out by the two instances in which a Chain Principle Offer price was determined in this case. But, as stated previously, this does not mean that the object of the exercise is any different; and nor does it mean that inconsistent methodology is employed.
82. The core problem in this case is to identify the data or the particular approach that most effectively points to the price to be paid by Disney and received by Fox's shareholders for Fox's 39% stake in Sky.
83. For reasons already summarised, the Independent Committee contends that the "linear approach" would be most effective to capture the price that will actually be received by the shareholders of Fox for their interest in Sky. As already noted, the Committee saw the attractions of this approach in the unique circumstances of this case. Ultimately, however, we concluded that the arbitrary nature of the exercise rules it out. By increasing the initial Chain Principle Offer price by a percentage equal to that by which the consideration payable under the Initial Acquisition Agreement increased under the Revised Acquisition Agreement, one proceeds on the assumption that the value of the stake in Sky (as perceived by Disney) increased precisely in line with the value of Fox's other assets. But there is no reason to believe that that was the case. For its part, Disney maintained strenuously that the process of negotiation simply involved redistributing between purchaser and seller the synergies anticipated from integrating Fox's US assets with Disney's existing business. One must also bear in mind that Fox was no doubt assisted in renegotiating the price by the fact that on 13 June 2018 Comcast had published a proposal to acquire Fox on the same basis as Disney but at an implied price of \$35.00 per share – a price which compared very favourably with the implied price of \$28.00 per share payable under the Initial Acquisition Agreement. For their part, the Shareholder Group contended that during

the period between Initial and Revised Acquisition Agreements the rate of increase in value of Fox's stake in Sky outstripped that of Fox's other assets. As support for this contention the Shareholder Group relied upon the factors to which Greenhill drew the Committee's attention and which are summarised above. But the truth is that one simply does not know the perceived relative increase in value of Fox's assets during the period in question. One can, however, say with some confidence that the stake in Sky is unlikely to have increased in value precisely in proportion to the increase in value of Fox's other assets.

84. There are also conceptual difficulties in adopting the linear approach advocated by the Independent Committee. One has to be certain that one is comparing like with like having stripped out anomalies. The Initial Acquisition Agreement involved an exchange of shares under which the implied cash equivalent depended on the volume weighted average price of Disney shares over the thirty days prior to the date on which the ratio was fixed. The Revised Acquisition Agreement involved an option to take part of the consideration in cash with the share exchange ratio floating within a fixed range (the collar arrangement). In the meantime, the Disney share price had increased significantly, something which would contribute to the increase in the cash equivalent of the revised consideration. The movement of exchange rates would also complicate the comparison. In summary, one cannot be sure that a ratio of \$28.00 to \$38.00 provides a reliable guide for an increase in the value attributed to Fox's stake in Sky. Finally, the linear approach depends upon accepting £10.75 per share as a basis for extrapolating to the revised price for each share in Sky; yet Disney maintained that this substantially exceeded its initial valuation of the 39% stake in Sky and was a figure accepted only because it reflected Fox's contemporary bid for the remaining shares of Sky.
85. The Committee was less attracted to the variant of the linear approach advocated by Greenhill, not out of any resistance in principle to an exercise which proceeds by reference to the increase in enterprise values, but because the outcome is skewed by assuming that Sky's net debt remained constant between the dates in question. The Committee was told by Fox at the hearing that when Greenhill's exercise is reworked using the updated figures for Sky's increased net debt, the result is a price per share of £14.10. Furthermore, adjusting the suggested price of £15.01 to take account of particular factors alleged to affect the relative value of the stake in Sky and Fox's other assets, is a highly speculative exercise. Selecting the factors to take into account (or, as the case may be, to omit) is itself a subjective exercise, as is interpreting the impact on price of any such factor. Greenhill implicitly recognised this in suggesting that the Executive currently had insufficient material to enable it to determine a Chain Principle Offer price.
86. There is no perfect way in this case to identify the value actually receivable by the shareholders of Fox for their interest in Sky. The Committee has come to the conclusion, however, that the most reliable piece of evidence for inferring the value attributed by Disney to Fox's stake in Sky from the consideration payable under the Revised Acquisition Agreement, is the price at which Disney subsequently authorised Fox to bid for the remaining shares of Sky on 11 July 2018. In authorising and supporting this bid, Disney agreed to take on the increase in debt which Fox would have to incur to make the offer. Disney also undertook to indemnify Fox for liabilities attributable to the offer price exceeding £13.00 in the event the acquisition of Fox did

not complete for regulatory or for some other specified reasons. Admittedly, this bid was made three weeks after the announcement of the Revised Acquisition Agreement, but in the Committee's view this does not prevent the offer price authorised and supported by Disney from being a good indication of the value per share in Sky which Disney had previously attributed in agreeing the consideration payable for Fox's assets. In the Committee's view, the fact that the Fox offer price was authorised and supported shortly after the announcement of the Revised Acquisition Agreement means that it has real value as evidence for inferring, retrospectively, the value which Disney had attributed to the 39% stake in Sky when agreeing the increased consideration payable under the Revised Acquisition Agreement.

87. Elliott points out, correctly, that the Fox offer of 11 July 2018 was for the remaining shares of Sky and was an offer made by a party which already held what the Code deems to be a controlling interest. Elliott goes on to contend that the price offered for the remaining 61% of the ordinary shares in Sky must logically be less than the price attributable to obtaining a controlling interest of 39%. This argument does not hold good, however, in the particular circumstances of this case where, in the face of a competing and, at the time, recommended bid by Comcast, an offer by Fox for the remaining shares indicated the price of consolidating or securing practical control over Sky. In such circumstances there is no reason why Fox's offer price for the remaining shares in Sky should be less than the price attributed by Disney to acquiring Fox's 39% stake.
88. Under Rule 9 of the Code it is the price paid to gain or consolidate a controlling interest that must, in turn, be offered for the remaining shares. Consistently with this, the Chain Principle Offer price should reflect the price attributed by Disney and received by Fox's shareholders for Fox's 39% stake in Sky. That, in turn, becomes the price which Disney has to offer to the other shareholders of Sky. As noted previously, the Committee believes that the price attributed by Disney to acquiring Fox's 39% stake in Sky under the Revised Acquisition Agreement, will have been driven by two principal factors, namely, the trading performance of Sky during the period since the Initial Acquisition Agreement and the strategic value to be attached to the 39% stake in circumstances where Disney was intent upon securing effective control of Sky in the face of a competing bid from Comcast.
89. Such considerations are, in the Committee's view best reflected in the offer price of £14.00 per share authorised and supported by Disney shortly after the Revised Acquisition Agreement had been announced. A Chain Principle Offer price of £14.00 is considerably higher than Disney's own revised DCF valuation of £11.80 per share and is consistent with the other valuation material made available to and considered by the Executive at the time. In addition, the price of £14.00 per share captures the enhanced value of acquiring a 39% stake in Sky in light of the competition for effective control which had developed by the time of the Revised Acquisition Agreement.
90. It is important to note that the fact that the Committee has given weight to the Fox offer price of 11 July 2018 as evidence for inferring the value previously attributed by Disney to Fox's stake in Sky in the consideration payable under the Revised Acquisition Agreement, does not mean that any later increased bids by Fox may be similarly relevant to the Chain Principle Offer price. The object of a Chain Principle

Offer is to ensure that the price actually received from A by the shareholders of B for B's interest in C is offered by A to the other shareholders of C once A completes its acquisition of B. Accordingly, unless the consideration payable for Disney's acquisition of Fox is again adjusted, no further bids by Fox will be relevant to determining the Chain Principle Offer price. In contrast to the bid of 11 July 2018, which the Committee views as reflecting a recent agreement to increase the consideration for acquiring Fox's assets, any future competitive bidding will not, in our view, have such relevance.

91. It remains to address the contention of the Shareholder Group that the matter should be remitted to the Executive with directions to determine a Chain Principle Offer price with the assistance of expert evidence and in accordance with directions given by the Committee. Determination of a Chain Principle Offer price by an independent expert would have to be sanctioned by the Code Committee of the Takeover Panel after a public consultation process. In this case the Shareholder Group does not suggest that an independent expert opinion should be determinative, simply that it should provide guidance for the Executive in its deliberations. The Committee believes, however, that such a procedure might compound rather than alleviate the problem of determining the value attributed by Disney to acquiring Fox's stake in Sky. Expert evidence would itself be open to challenge and would do no more than provide a range of values without removing scope for substantial argument. Furthermore, the core questions in this case are not amenable to resolution by expert evidence.
92. Accordingly, the Committee directs that the Chain Principle Offer which Disney will be obliged to make within 28 days of completing its acquisition of Fox should be at the price of £14.00 for each ordinary share in Sky, but that that offer need not be made if by then Fox has acquired 100% of the shares in Sky or Comcast or any other third party has acquired more than 50% of such shares.
93. The time for appealing this ruling to the Takeover Appeal Board is set out in the Rules of Procedure of the Takeover Appeal Board and will run from the date of delivery of this Ruling to the parties.

Dated 3 August 2018

Michael Crane QC

Signed by the Chairman on behalf of the Committee

**APPENDIX 1**  
**LIST OF PARTIES AND THEIR ADVISERS**

The parties who made submissions to the Hearings Committee were:

<b>Party</b>	<b>Advisers</b>
Sky Plc	Morgan Stanley PJT Partners Barclays Herbert Smith Freehills LLP
Twenty-First Century Fox Inc.	Deutsche Bank Allen & Overy LLP
The Walt Disney Company	Citibank Slaughter and May
Elliott Advisors (UK) Limited	Michael Todd QC (Erskine Chambers) Simmons & Simmons LLP
Davidson Kempner European Partners, LLP	Greenhill & Co. International LLP (Common Representative)
Farallon Capital Europe LLP	
Elliott Advisors (UK) Limited	
P Schoenfeld Asset Management LLP	

**APPENDIX 2  
HEARINGS COMMITTEE MEMBERS**

The members of the Hearings Committee who constituted the Committee for the purpose of the Hearing were:

<b>Individual's Name</b>	<b>Position or Firm</b>
Michael Crane QC	Chairman
Philip Remnant	Deputy Chairman
Justin Dowley	Deputy Chairman
Mark Seligman	Royal Bank of Scotland
Martin Mannion	John Lewis Partnership Pensions Trust
Peter Swabey	ICSA
Tim Ward	Quoted Companies Alliance
<b>Secretary to the Hearings Committee</b>	
Helen Bradley	Baker McKenzie