bvca The voice of long-term investment

BVCA response to BIS consultation on 'A long-term focus for corporate Britain'

About the BVCA: The British Private Equity & Venture Capital Association (BVCA) is the industry body and public policy advocate for the private equity and venture capital industry in the UK.

The BVCA Membership comprises over 230 private equity, midmarket and venture capital firms with an accumulated total of approximately £32 billion funds under management; as well as over 220 professional advisory firms, including legal, accounting, regulatory and tax advisers, corporate financiers, due diligence professionals, environmental advisers, transaction services providers, and placement agents. Additional members include international investors and funds-of-funds, secondary purchasers, university teams and academics and fellow national private equity and venture capital associations globally.

As a result of the BVCA's activity and reputation-building efforts, private equity and venture capital today have a public face. Venture capital is behind some of the most cutting-edge innovations coming out of the UK that many of us take for granted: the medical diagnostic services we use in hospitals, the chips in our mobile phones, the manufactured components of our cars, and the bioethanol fuels that may run them in the future. Likewise, private equity is behind a range of recognisable High Street brands, such as Boots, Phones4U, Birds Eye, National Grid and Travelodge.

Whilst this consultation is directed at listed companies and interactions between their boards and shareholders, the private equity industry has a vested interest in the operation of the takeover regulations governing those companies.

Takeovers

The BVCA's starting position is that proposed revisions to the Takeover Code by the Takeover Panel are a dramatic intervention with the potential to hugely impact on takeover activity and economic growth. We believe these reforms go too far for reasons outlined below but in this context, it must be stressed that any attempt to extend these changes by other means are wholly unnecessary. The BVCA remains concerned that in an attempt to protect and indeed maximise shareholder value, some of the reforms proposed both by the Takeover Panel in their consultation and those in this consultation may have unintended consequences, particularly with respect to the attempts to rebalance the playing field in favour of the offeree company.

- **Naming and 4 week period:** All potential bidders are to be named in the first announcement which identifies that a takeover approach has been made. This has the potential to deter potential bidders and therefore ultimately detract from shareholder value. Although it may prevent so called fishing expeditions and speculative bidding many potential bidders will be put off entirely. Will potential bidders, who have not yet had time to make sufficient progress with their investigations into the target (and mindful of the four week timetable), choose instead to withdraw before they are named? That being the case there is clearly scope for detraction of shareholder value. Furthermore if a 4 week limit is rigidly imposed, this will deter legitimate bidders who simply cannot conduct what may be multi-jurisdictional due diligence fast enough.

- **Fees:** Except where the target has initiated a formal process for its sale by means of a public auction, inducement (break) fees and all deal protection measures (such as non-solicitation of other bidders and matching rights) will be prohibited. Yet there is no evidence that

inducement fees deter potential competing bidders, particularly as under the current rules they are capped at 1% of the offer price. In addition, certain types of bidder may not make a bid unless they have some cost protection in the event that they are out-bid. Since that might stop offers being put to shareholders, and given that the fee is only ever paid by the successful bidder if payable in such circumstances, it is likely to be beneficial to the target shareholders and it is hard to see how that can be prejudicial to other stakeholders. Given that most respondents to the Panel's original consultation, including those representing listed companies consider that the current rules on inducement fees are satisfactory, it is unclear on what basis there is to intervene in this area or why there is a working assumption that a public company board is unable to negotiate commercial arrangements for itself

- **Disclosure of financial information:** Greater details of the bidder's financial position and of its financing of the offer will need to be disclosed than at present, including a *pro forma* balance sheet of the combined bidder/target group. It has not yet been formally confirmed that such disclosure will not extend above the bid vehicle in the case of private equity bids; for example, to other portfolio companies. But how deep are the disclosure requirements likely to be for debt facilities and will redactions of financing documents be permitted? Again if too much is demanded by way of disclosure in the name of protecting target companies it may deter potential bidders to the obvious detriment of shareholder value.

We operate under the continuing assumption that company boards are best placed to look after the interests of their shareholders that the protections afforded them by existing arrangements are necessary but sufficient. If there are issues to be resolved in how a board promotes shareholder value, we would suggest that these should be resolved via internal corporate governance reform rather than changes that will simply deter legitimate bids from being tabled.

Questions

15) Do boards understand the long-term implications of takeovers, and communicate the long-term implications of bids effectively?

16) Should the shareholders of an acquiring company in all cases be invited to vote on takeover bids, and what would be the benefits and costs of this?

Bolstering the requirement to consult with or indeed get positive assent from shareholders does not change the nature of the problem and that is that the responsibility for managing the strategic direction of the company rests with the board and they remain best placed to do that. Directors of an acquiring company who do not understand the long-term implications of a proposed takeover which they wish to undertake may nevertheless recommend it to their shareholders. The recommendation has a strong influence on shareholders who will, in most cases, be less well placed than the directors to make a proper and informed assessment of the transaction. It may require the directors to think more carefully in all circumstances about how they articulate their rationale for the transaction but we don't believe it would necessarily change the rationale.

The question of whether listed acquirers should be required to vote in a takeover consultation again does not directly concern BVCA members. However an assurance that in the case of a takeover bid

from a discretionary managed fund no vote/consent would be required by investors would be helpful since it would be legally impossible to obtain because of the limited liability arrangements governing the fund.