March 13, 2023

Amendments to UK Takeover Code

Five Key Takeaways for Financial Sponsors From Changes to "Acting in Concert" Presumptions

BACKGROUND

On February 20, 2023, the UK's Panel on Takeovers and Mergers (the "**Panel**") amended the City Code on Takeovers and Mergers (the "**Code**") in relation to the circumstances in which persons will be presumed to be "acting in concert" with each other under the Code. A particular focus of the amendments has been to set out clearly how the "acting in concert" presumptions apply to financial sponsors and their limited partners.

The amendments follow a consultation that started in May 2022 and a response to the consultation published by the Panel in December last year.

KEY TAKEAWAYS FOR FINANCIAL SPONSORS

1. NEW "ACTING IN CONCERT" PRESUMPTIONS INTRODUCED; NO ABILITY FOR FINANCIAL SPONSORS (OR ANYONE ELSE) TO USE COMFORT LETTERS TO DISAPPLY PRESUMPTIONS IN RELATION TO NON-CONTROLLED PORTFOLIO COMPANIES

The previous presumption that two (or more) companies were acting in concert if one of them owned or controlled 20% or more of the equity share capital of the other has been replaced by two new presumptions:

- Presumption 1: a company (X) and any company which controls, is controlled by or is under the same control as X are all presumed to be acting in concert with each other. "Control" means being interested in either shares carrying 30% or more of the total voting rights of the other company or a majority of the equity share capital of the other company.
- Presumption 2: a company (Y) and any other company (Z) are presumed to be acting in concert with each other where one of Y or Z is interested, directly or indirectly, in 30% or more of the equity share capital of the other (whether or not the shares carry voting rights); any company which would be presumed to be acting in concert with either Y or Z under presumption 1 is also presumed to be acting in concert with Y and Z under presumption 2.

The Panel had previously been willing to disapply the presumption that named 20% to 50% portfolio companies were acting in concert with the bidder on receipt of a comfort letter from the relevant financial

sponsor. Such comfort letters would contain standard form confirmations required to give the Panel comfort around the portfolio companies' independence from the sponsor, and a list of the relevant portfolio companies in respect of which the accommodation was being sought would be annexed to the letter. The Panel has not carried over this practice to these new presumptions 1 and 2 above. As a result, financial sponsors should proceed on the basis that portfolio companies where they (i) control 30% or more of the voting rights or (ii) are interested in 30% or more of the economics, will now be presumed to be acting in concert with the bidder.

The Panel has indicated that it may be willing, on a case-by-case basis, to rebut presumptions 1 and 2 in respect of portfolio companies in which a single third party is interested in more than 50% of the voting rights or equity share capital (as applicable), on the basis that the relevant financial sponsor does not, in fact, control the portfolio company. Financial sponsors will, therefore, need to consider whether they would apply to the Panel to rebut the presumptions in respect of such portfolio companies at the outset of any takeover transaction. This will require weighing the administrative burden of providing the Panel with detailed information on those portfolio companies' shareholding structures against the comfort that, if the presumption is rebutted, dealings in target shares by those portfolio companies will not be potentially capable of setting a floor price for the offer or requiring a particular form of consideration to be offered (i.e., cash or shares), or triggering a mandatory offer. For most financial sponsors, however, the number of portfolio companies where these presumptions can be rebutted will be relatively limited, and the work required to rebut the presumptions will be greater than was previously involved in providing a standard comfort letter to the Panel.

2. NEW PRESUMPTIONS APPLY TO LIMITED PARTNERS

Presumptions 1 and 2 apply not just to companies but to any undertaking (including a partnership or trust) or any legal or natural person. In particular, they apply to limited partnership interests in a fund in an equivalent manner as they apply to non-voting equity share capital in a company:

- A limited partner will be presumed to be acting in concert with the fund if the limited partner either: (i) is interested in more than 50% of the limited partnership interests in the fund (presumption 1); and/or (ii) has a "see through" interest in 30% or more of the limited partnership interests (presumption 2).
- Where the fund invests in a new bid vehicle ("**Bidco**") formed for the purpose of making an offer for a Code company, a limited partner in the fund will be presumed to be acting in concert with Bidco if the limited partner either: (i) is interested in more than 50% of the limited partnership interests in the fund (presumption 1); and/or (ii) has a "see through" indirect interest in 30% or more of the equity share capital of Bidco (presumption 2).

Financial sponsors will therefore need to ascertain whether any limited partners hold sufficient limited partnership interests such that they would be presumed to be acting in concert with their funds or any Bidco under presumption 1 or 2. Where the financial sponsor is bidding alone, this should usually be simple to ascertain as the limited partner would need to hold a 30% (or larger) interest in the relevant fund.

The position is more complicated in a consortium bid. This is because indirect interests in a fund or Bidco need to be aggregated when determining whether new presumption 2 is satisfied. As a result, in a consortium bid with multiple financial sponsors, the consortium members will need to agree a process with each other to assess whether any limited partner (via being a limited partner in multiple consortium members) has indirect interests in Bidco that, when aggregated, may cause the limited partner to be indirectly interested in 30% or more of Bidco.

As a special case, if a limited partner's investment in Bidco is structured through a separate fund that invests in parallel with the main fund, then, provided both funds are managed on a unified basis, the new presumptions will be applied to the limited partner in a different way. Firstly, as a derogation from the usual application of presumption 1, the limited partner will not be presumed to be acting in concert with Bidco by virtue of being interested in 50% or more of the limited partnership interests in the separate fund. Secondly, in order to calculate the limited partner's indirect interests in Bidco for the purposes of presumption 2, the separate fund and the main fund will be treated as if they are a single fund.

A limited partner who is presumed to be acting in concert with a fund or Bidco will need to agree not to deal in target shares during the offer period and any target shares held (directly or indirectly) outside of the bidding consortium will need to be identified. Given the risk that limited partners may be unwilling, or unable, to enter into such discussions and agreements, it is expected that early identification of relevant limited partners and consultation with the Panel will be crucial.

3. MAKING A POSITIVE DECISION TO INVEST IN A BIDCO WILL TRIGGER "ACTING IN CONCERT" PRESUMPTION

Presumptions 1 and 2 apply to limited partners in their capacity as passive investors in funds that are managed on a discretionary basis. Where a limited partner (or other investor) makes a positive decision to invest in a Bidco (i.e., otherwise than through a fund managed by the sponsor), including by exercising a co-investment right or by participating in an equity syndication, it will be presumed to be acting in concert with Bidco regardless of the size of its interest in the fund or its indirect interests in Bidco.

Where such a limited partner (or other investor) is part of a larger organisation, there will be a rebuttable presumption that its larger organisation is also acting in concert with Bidco (see point 5 below).

4. LIMITED PARTNERS' IDENTITIES AND DETAILS OF THEIR INTERESTS IN THE TARGET MAY NEED TO BE DISCLOSED

Financial sponsors will need to be prepared to disclose the identity of limited partners that are presumed to be acting in concert with them. Disclosure will be required if the limited partner:

- has an interest in target securities at the outset of the offer period;
- has dealt in target securities either in the 12 months prior to, or during, the offer period; or
- has an indirect interest of 5% or more in the target as a consequence of the transaction.

5. THRESHOLD WHERE PRESUMPTIONS MAY BE DISAPPLIED IN RESPECT OF FINANCIAL SPONSORS' LARGER ORGANISATIONS REDUCED FROM 50% TO 30%

The Panel may be willing to disapply the presumption that the larger organisation of a financial sponsor (or other person) that invests in a Bidco is acting in concert with Bidco. The Panel will normally disapply the presumption if the relevant fund's interest in Bidco is less than or equal to 10%, provided it is satisfied of the independence of the larger organisation from the fund. The Panel may also be prepared to disapply the presumption if the fund's interest is more than 10% but less than 30%. This 30% threshold was previously set at 50%.

Subject to the same thresholds, the Panel may also be willing to disapply the presumption that the following are acting in concert with Bidco:

- the larger organisation of any limited partner in a fund that is presumed to be acting in concert with such fund by virtue of presumption 1; and
- the larger organisation of any investment manager or investment adviser to a fund that is presumed to be acting in concert with Bidco.

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