

## CORONAVIRUS RESOURCE CENTER

# Public-to-Private Transactions in the UK— Key Considerations for Sponsors in the Current Environment

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## INTRODUCTION

As global financial markets continue to feel the strain of the COVID-19 pandemic, M&A activity has reduced significantly. But with private equity sponsors sitting on record levels of capital commitments, the recent fall in public company equity values presents an opportunity for sponsors to deploy some of this capital. 2019 saw a notable rise in the number of public-to-private transactions in the United Kingdom, the number of such deals increasing by 40% compared to 2018.<sup>1</sup> Although such growth may not be repeated this year, the combination of reduced share prices, record-low UK interest rates and capital commitments available to sponsors for investment could lead to an uptick in public-to-private activity in the rest of 2020.

This client update explores some of the key considerations sponsors should bear in mind as they consider undertaking a public-to-private transaction involving a UK-listed target against the backdrop of the COVID-19 crisis, with a focus on what is different in the current economic and political climate.

## KEY CONSIDERATIONS

- **Pricing.** Establishing the right price for a company whose share price has fallen significantly since the start of the COVID-19 pandemic is not a straightforward task, particularly for foreign investors considering opportunities whilst global currencies are also in a state of flux. Target companies operating in certain sectors that have been hit particularly hard, such as transport, tourism and hospitality, may be even more difficult to value at this time. This task is made even more challenging in

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<sup>1</sup> PE News: *No end in sight for UK take-privates as deal value more than doubles in 2019.*

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respect of targets that may be in need of additional liquidity support, at a time when auditors may be uncomfortable giving “going concern” audit opinions. Sponsors should also be sensitive to target boards as well as selling shareholders who, having already suffered acute paper losses on their investments, may be unreceptive to offers perceived to be exploiting current uncertainty. With current levels of volatility, there is also a chance that share prices move generally up, such that a public offer no longer provides as much of a premium - or perhaps no premium at all - to the trading price at the launch of an offer. Unlike private M&A deals and/or on-market purchases of smaller stakes in public companies, public offers have a minimum price for a minimum duration, introducing execution risk. Messaging around and justification of valuations (to target boards, selling shareholders and limited partners) are more important for sponsors than ever.

- **Scrutiny of Foreign Investments.** Sponsors based outside the UK should be aware of recent moves towards greater levels of scrutiny of takeovers by foreign investors of strategically important companies, including those operating in industries such as the infrastructure, defence, technology and healthcare sectors. In line with approaches being taken in a number of jurisdictions, the UK government has put forward far-reaching proposals for a regime - separate from merger control - to review a much broader range of transactions (or “trigger events”), including takeovers, which might raise national security concerns. This regime, were it to come into force, would impact a number of transactions and their timetables and follows on from changes already made in 2018 to the existing government powers to allow it to intervene in the military and dual-use, computing hardware and quantum technology sectors. These powers have already been used in a number of cases, including several involving financial sponsors (e.g., the acquisition of Inmarsat by a consortium led by Apax Partners and Advent International’s acquisition of Cobham). The European Commission is also taking steps to protect the European Union’s security and economic sovereignty in the context of foreign direct investments, further information on which is available [here](#).
- **Due Diligence.** In light of lockdown and travel restrictions (which may persist post-lockdown) imposed by governments in response to the COVID-19 pandemic, sponsors’ ability to mobilise due diligence teams, meet in person with a target’s management team, or visit key sites or operations as part of the due diligence process is significantly impacted. While technology provides an alternative (e.g., videoconferencing with management or virtual tours of key sites), it is not an absolute solution. Sponsors and their advisers will need to think creatively around these practical issues in conducting due diligence.
- **Availability of Acquisition Financing.** Given the level of volatility in global markets at present, lenders are less willing to commit to provide debt financing in

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part due to the difficulty of predicting the financial performance of target businesses, and ultimately their ability to repay the debt in the future. This, coupled with the requirement under the City Code on Takeovers and Mergers (the “Code”) for acquisition financing to be provided on a “certain funds” basis (with extremely limited “outs”), could result in a scarcity of available acquisition financing for public-to-private transactions.

- **Conditionality.** While the private M&A market has seen the introduction of COVID-19 specific provisions in deal documents, providing purchasers protection in the event of material impacts on the target business as a result of the COVID-19 outbreak, sponsors should be aware that the UK Panel on Takeovers and Mergers is unlikely to allow an offeror to rely on COVID-19-related conditions to walk away from an offer once it has been announced - any “material adverse change” (“MAC”) after an offer is made must be so substantial that it strikes at the heart of the target business for an offeror to rely on such a MAC condition. A known risk such as COVID-19 is unlikely to meet such a high threshold. This risk is magnified by potentially extended deal timelines, as discussed below.
- **Extended Deal Timelines.** In the event that any regulatory or merger control conditions - whether in the UK or elsewhere - must be satisfied prior to completion, deal timelines in the current climate are likely to be extended, increasing execution risk as a result. Most significant merger control authorities across the globe have confirmed that, as a result of remote working and the practical challenges of undertaking market investigations, average review times for merger control applications have been increased. The same is true for certain industry regulators. Sponsors should consult with legal counsel at an early stage of any proposed transaction to ensure that any requisite merger control or regulatory filings are navigated as efficiently as possible.
- **Stakebuilding.** Often bidders for public targets seek to increase the likelihood of success of their bid, particularly in competitive scenarios, by building a stake in the target. Sponsors should not consider market purchases of target shares to be independent from the terms of an eventual offer - under the Code, if a bidder or its concert parties acquire an interest in shares in the target during the three months prior to the offer period or during any period between the commencement of the offer period and the announcement by the bidder of an intention to make an offer, then the offer must not be on less favourable terms (i.e., any such purchases set a “floor” on the price the bidder may offer). In times of market volatility, where prices may continue to fall, being bound to offer a minimum price could hinder a sponsor’s ability to strike a deal on the most attractive terms.

- **Special Issues for Schemes of Arrangement.** The most effective and hence most common structure for take-private transactions in the UK is a scheme of arrangement. Schemes of arrangement enable the acquisition of 100% ownership of a UK public target. However, such structure requires shareholder approval at a general meeting of shareholders and court approval, both facing procedural changes in current circumstances.
- **Holding of Shareholder Meetings.** UK-listed companies have been adapting their practices for the holding of shareholder meetings, with some companies opting to hold “virtual” meetings and encouraging all shareholders to vote by way of proxy. Changes to regular corporate procedure should be factored into transaction timelines.
- **Holding of Court Hearings.** Either side of the shareholder meeting to approve a scheme of arrangement, court hearings are held to direct the convening of the shareholder meeting and grant an order sanctioning the scheme. Like UK-listed companies, UK courts have had to transition towards virtual hearings in recent weeks, a concept that is not completely novel for UK courts.

## CONCLUSION

While public-to-private transactions involving UK-listed companies have become more prevalent in recent years, there are a number of pitfalls unique to the current economic environment that sponsors should keep at the forefront of their minds when evaluating such transactions. This becomes even more important at a time when record levels of committed capital are available to sponsors looking to seize opportunities to invest in (perhaps temporarily) undervalued assets.

We would be happy to discuss this topic or any questions you may have or issues you may be facing in connection with current or prospective take-private processes.

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For more information regarding the coronavirus, please visit our [Coronavirus Resource Center](#).

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