

RS 9 Issued on 4 July 2002

THE PANEL ON TAKEOVERS AND MERGERS

**QUESTIONS AS TO THE POTENTIAL
CONCERTEDNESS OF THE TRUSTEES OF AN
EMPLOYEE BENEFIT TRUST WITH THE BOARD
AND/OR A CONTROLLING SHAREHOLDER**

**STATEMENT BY THE CODE COMMITTEE OF THE
PANEL FOLLOWING THE EXTERNAL
CONSULTATION PROCESS ON PCP 9**

1. Introduction

- 1.1 On 14 March 2002, the Code Committee of the Takeover Panel published a Public Consultation Paper (PCP 9) on questions as to the potential concertedness of the trustees of an Employee Benefit Trust and the Board of a company and also that of the trustees and a controlling shareholder.
- 1.2 The proposals in PCP 9 sought to add a new Note 5 to Rule 9.1 to address the circumstances in which trustees would be deemed to be acting in concert with the directors or a controlling shareholder for the purposes of the Code. It was also proposed that a new Note 5 should be added to SAR 5 to make it clear that where parties were considered to be acting in concert pursuant to the new Note 5 on Rule 9.1, they would also be considered to be acting by agreement or understanding for the purposes of SAR 5.
- 1.3 The purpose of this paper is to provide details of the Code Committee's response to the external consultation process on PCP 9.

2. Number of responses received

A total of 9 responses was received, mainly from major industry bodies and practitioners.

3. Significant conflicts of views

There was general support for the overall approach towards potential judgements of concertedness and the factors to be taken into account in making those judgements. However, a majority of respondents disagreed with the specific proposal that the trustees should be deemed to be acting in concert with the board when the directors themselves were deemed to be acting in concert. Similarly, there was a majority against the proposal that the trustees should be presumed to be acting in concert with a controlling shareholder where the controlling shareholder in fact exerted a dominant influence over the board. Two respondents asked for special treatment for a particular type of EBT, the All-Employee Share Scheme.

4. The Code Committee's conclusions

4.1 Question 1: Do you agree that there should not be a general presumption that the trustees and directors are acting in concert? and

Question 2: Do you agree that the independence or otherwise of the trustees should not be a conclusive factor in determining whether the trustees should be deemed to be acting in concert with the board?

4.1.1 There was general agreement with both these propositions. Some respondents suggested that each case should be judged on its merits. The Code Committee totally accepts this and believes it is implicit in the wording of new Note 5 on Rule 9.1, which states that the Panel will consider '*all relevant factors*'.

4.1.2 Another respondent felt that trusts which have tax approval and are operated on an 'all-employee' basis, in accordance with applicable tax legislation, should not be regarded as 'Employee Benefit Trusts' for the purposes of ascertaining whether they form part of a concert party since the trustees are constrained by that legislation. In particular, the trust deeds do not permit them to benefit only directors or members of a shareholder's family. The Code Committee was aware, in putting forward its proposals, that there are a number of different types of EBT but it did not consider that there was any need to make special provision for them. The requirement for the Panel to consider 'all relevant factors' will ensure that any special circumstances relating to an EBT will be taken into account in decisions as to concertedness.

4.1.3 It was also suggested that there should be some guidance as to the meaning of 'independence'. The Code Committee believes that the factors listed in the new Note 5 all contribute towards determining the independence of the trustees and there is no need to give further guidance, especially since the concept of 'independence' per se is not referred to in the Note.

4.2 Question 3: Do you consider that:

(i) each of the factors in paragraph 5.5 is relevant [to judgements of concertedness];

(ii) there are any other factors which should be considered?

4.2.1 Most respondents were content with the list of factors proposed. There were two suggestions for additions to the list. One respondent felt that it would be useful to compare the timing of the decision of the company to make awards under the scheme and/or the decision of the trustees to buy shares with the actual timing of the purchases by the EBT. The Code Committee agrees that timing is an issue but feels it is catered for in factors (c), (f) and (g) in paragraph 5.5 and does not need to be referred to explicitly. If, however, an EBT proposes to deal in shares in the company during an offer period, it should consult the Panel before doing so.

4.2.2 One of the factors proposed was *‘the percentage of the issued share capital held by the EBT’* and PCP9 suggested that if the percentage exceeded the 5% threshold set by the ABI, that could be a significant factor. One respondent commented that if the shareholders had voted to approve the percentage of shares held by the EBT, then this factor should not be relevant, even if it exceeded the 5% threshold. The Committee accepts this view and would expect the Panel to interpret the provision accordingly.

4.2.3 Another respondent suggested that it could be useful to consider previous voting patterns of the trustees. The Code Committee agrees that this could be significant. It could indeed be useful to see whether, for example, the trustees always voted in accordance with the wishes of the board and/or a controlling shareholder, or if, by contrast, they had a policy to abstain. The Code Committee believes this factor should be added to the list of relevant factors in the new Note 5 on Rule 9.1 in the following terms:

“any established policy or practice of the trustees as regards decisions to acquire shares or to exercise votes in respect of shares held by the EBT;”

4.3 Question 4: Do you agree that the trustees should be deemed to be acting in concert with the board when the directors themselves are deemed to be acting in concert?

4.3.1 A large majority of the respondents was opposed to this proposal. Some acknowledged that in circumstances where the trustees were themselves directors or were influenced by the directors, then a presumption of concertedness might be appropriate. But overall, the strong feeling was that each case should be judged on its particular circumstances. The Code Committee accepts the strength of feeling on this point and has, therefore, decided to remove the presumption, deleting the proposed fourth paragraph of new Note 5 on Rule 9.1. It nonetheless feels that the fact of the directors themselves being presumed to be in concert would be a significant factor for the Panel in making any overall judgement about the inclusion in any concert party of the trustees of the EBT. It has, therefore, also decided to add a further item to the list of relevant factors in the Note as follows:

“whether or not the directors themselves are presumed to be in concert;”

4.3.2 Two respondents commented on whether the trustees should be ‘presumed’ to be in concert with the directors or ‘deemed’ to be so. The PCP and the proposed Note had used these terms interchangeably. The respondents’ concern was that the trustees should be able to rebut any such presumption or deeming. Having deleted the presumption from the Note, the Code Committee now believes that the last sentence of the second paragraph should refer to neither presumption nor deeming, but should read as follows:

“Its consideration of these factors may lead the Panel to conclude that the trustees are acting in concert with the directors.”

4.4 Question 5: Do you agree that the trustees should be deemed to be acting in concert with a controlling shareholder where the controlling shareholder in fact exerts a dominant influence on the board?

4.4.1 This question provoked a similar reaction to Question 4. A majority of respondents was opposed to a presumption of concertedness of the trustees with a controlling shareholder. There was recognition that all the relationships (trustees/board, shareholder/board, shareholder/trustees) needed to be considered but some expressed doubt about how easy it would be to test whether a shareholder in fact exerted a dominant influence over the board. One respondent felt that a controlling shareholder should not be treated as in fact exerting a dominant influence over the board if, as was suggested in PCP9, one holder of significant office was a representative of or closely connected with that shareholder.

4.4.2 The Code Committee accepts these views and, accordingly, has decided to remove this presumption as well, deleting the proposed third paragraph of new Note 5 on Rule 9.1. However, in circumstances where there is a controlling shareholder, or group of shareholders, the Panel will wish to consider the relationship between that shareholder (or group) and both the board and the trustees. The Committee, therefore, wishes to emphasise the importance of the requirement in the Note to consult the Panel in any case where there is a controlling shareholder or group of shareholders and the EBT plans to acquire shares. It has also decided to amend new Note 5, so that the first sentence of the second paragraph of the Note will read:

“ The mere establishment and operation of an EBT will not by itself give rise to a presumption that the trustees are acting in concert with the directors and/or a controlling shareholder (or group of shareholders acting, or presumed to be acting in concert).”

Another item will then be added to the list of relevant factors as follows:

“the nature of any relationship existing between a controlling shareholder (or group of shareholders acting, or presumed to be acting in concert) and both the directors and the trustees.”

The following words will then be added at the end of the last sentence of the paragraph :

“and/or a controlling shareholder (or group).”

4.5 Question 6: Do you agree that any presumption of concertedness should not apply to shares held within the EBT but controlled by beneficiaries?

4.5.1 Respondents were generally in agreement with this proposal. One respondent felt that more guidance might be needed depending on the rules of the scheme. The Committee feels that this is adequately catered for by the need to consider ‘all relevant factors’.

4.6 Implications for SAR 5

4.6.1 One respondent made the observation that it would be strange to add a new Note to SAR 5, making specific reference to the particular activities described in the new Note 5 on Rule 9.1 and those proposed, in PCP10, in the revised Note 2 to Rule 9.1. The inclusion of such specific references might, it was felt, give the impression that persons who are presumed or deemed to be acting in concert for other reasons under the Code might not be considered to be acting ‘by agreement or understanding’ for the purposes of SAR 5. The Code Committee accepts that such an inference could be drawn from the new Note 5 on SAR 5 and that this would be undesirable. The Note will not, therefore, be added. However, practitioners should be aware that, by virtue of SAR 5, the SARs will be relevant to the purchase of shares by trustees of an EBT.

5. Amendment to the Code

The Appendix to this document sets out in full the text of the new Note 5 on Rule 9.1, as amended by the further changes discussed in this statement.

APPENDIX

Rule 9.1

NOTES ON RULE 9.1

5. *Employee Benefit Trusts*

The Panel must be consulted in advance of any proposed acquisition of new or existing shares if the aggregate holdings of the directors, any other shareholders acting, or presumed to be acting, in concert with any of the directors and the trustees of an employee benefit trust (“EBT”) will, as a result of the acquisition, equal or exceed 30% of the voting rights or, if already exceeding 30%, will increase further. The Panel must also be consulted in any case where a shareholder (or group of shareholders acting, or presumed to be acting, in concert) holds 30% or more (but not more than 50%) of the voting rights and it is proposed that an EBT acquires shares.

The mere establishment and operation of an EBT will not by itself give rise to a presumption that the trustees are acting in concert with the directors and/or a controlling shareholder (or group of shareholders acting, or presumed to be acting in concert). The Panel will, however, consider all relevant factors including: the identities of the trustees; the composition of any remuneration committee; the nature of the funding arrangements; the percentage of the issued share capital held by the EBT; the number of shares held to satisfy awards made to directors; the number of shares held in excess of those required to satisfy existing awards; the prices at which, method by which and persons from whom existing shares have been or are to be acquired; the established policy or practice of the trustees as regards decisions to acquire shares or to exercise votes in respect of shares held by the EBT; whether or not the directors themselves are presumed to be in concert; and the nature of any relationship existing between a controlling shareholder (or group of shareholders acting, or presumed to be acting in concert) and both the directors and the trustees. Its consideration of these factors may lead the

Panel to conclude that the trustees are acting in concert with the directors and/or a controlling shareholder (or group).

No presumption of concertedness will apply in respect of shares held within the EBT but controlled by the beneficiaries.”