The Sale of the British Technology Group
This report has been prepared under Section 6 of the National Audit Act 1983 for presentation to the House of Commons in accordance with Section 9 of the Act.

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National Audit Office
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Summary and conclusions

1 On 31 March 1992, following a competitive bidding process, the Department of Trade and Industry (the Department) sold British Technology Group (the company) for initial proceeds of £27.75 million to a consortium of investors led by the company’s management and employees (the management-led consortium). The initial proceeds consisted of payments of £13.5 million from the cash reserves of the company and a payment from the consortium of £14.25 million. The net assets of the company acquired by the consortium included £4.3 million cash.

2 The company’s business consists of technology transfer, that is the commercial exploitation of a wide range of inventions and new processes. The Government decided to privatise the company on the grounds that they were already operating on a commercial basis in an increasingly competitive international market place. The Department’s objectives for the sale were to maximise the net return to the taxpayer consistent with a good prospect of the continuation of the company’s technology transfer activities.

3 The National Audit Office examined whether the Department had
- identified the most appropriate method of sale
- valued the business in an appropriate manner
- considered suitable clawback provisions
- negotiated the sale on the best possible terms
- exercised effective control over the costs of sale.

i) Method of sale

4 The Department and their financial advisers reviewed a range of possible sale methods, against the background of assurances given to Parliament concerning safeguards that would be introduced to help secure the continuity and independence of the business. These included provision for the Secretary of State to hold a special share for up to five years after the sale, and for a 15 per cent limit on the proportion of voting shares that any one institutional investor could hold. The Department decided to offer the company for sale to groups of investors (consortia) since they saw this sale method as offering a good prospect of maximising competition for the company, consistent with securing continuity of the business (paragraphs 2.2 to 2.14).

Conclusion

5 The sale method adopted by the Department and the range of safeguards that they introduced were consistent with the sale objectives.
ii) Valuation

6 To provide a benchmark against which to evaluate bids, the Department's financial advisers carried out a valuation of the company in December 1991 which identified a valuation range of £15 million to £30 million. This assumed that the Department would receive £13.5 million from the company and leave £10 million cash in the business. To the extent that the cash balance on sale was less than £10 million, the valuation range would decrease on a £1 for £1 basis. The valuation covered a number of scenarios and took into account the constraints relating to the possible structure of bids (paragraphs 2.15 to 2.17). The Department also obtained an independent assessment of the company's likely future income from their portfolio of intellectual property assets and commissioned a valuation of the company's land and buildings (paragraphs 2.18 to 2.19).

Conclusion

7 The valuation approach and methodology were appropriate to the nature of the business being sold.

iii) Clawback provisions

8 The Department decided to introduce clawback provisions on gains from the disposal of land and buildings during the five year period after the sale. They also invited bidders to make proposals aimed at ensuring that the Government received benefit from any income arising from the company's existing portfolio of technologies in excess of the company's corporate plan projections (paragraphs 2.20 to 2.22).

Conclusion

9 The clawback on land and buildings was in line with previous privatisations. As regards income in excess of projections, the Department's approach offered the prospect of stimulating competitive bidding on this aspect of the sale, while leaving it to the bidders to address the scope and extent of any proposals.

iv) Negotiating the sale

10 In order to stimulate competitive bids, the Department's financial advisers met some 30 organisations who had expressed an interest in the sale, and sent details to some 200 more potential investors in the United Kingdom and overseas (paragraph 2.23).

11 In the first (indicative) round of bidding, four consortia submitted bids. These were within the valuation range of £15 million to £30 million (paragraph 2.27). In the second (formal) round of bidding the Department were concerned to guard against the risk of the management-led consortium having a greater access to information than the other bidders, and also to respect the confidentiality and sensitivity of data. The Department introduced rules and procedures, including the provision of a data room, to
permit all four consortia equal access to selected information (paragraphs 2.28 to 2.33). Two of the four consortia complained that the information provided was insufficient to enable them to submit formal bids (paragraph 2.34).

12 The company’s management still wished to withhold certain information about the terms of licences on grounds of confidentiality and commercial sensitivity, but the Department took further steps to make as much information as possible available to bidders (paragraphs 2.35 to 2.38). One of the consortia who complained withdrew from the sale. The other three consortia submitted formal bids (paragraphs 2.39 to 2.40). The Department decided to invite two of these, the management-led consortium and the Anglo-American consortium, to proceed to the final competitive bidding stage (paragraphs 2.41 to 2.43).

13 At the final competitive bidding stage, the management-led consortium bid £28.3 million, whilst also requesting up to £1 million from the Department to cover their costs. The Anglo-American consortium bid £30.4 million. Both consortia made proposals for clawback on income in excess of the corporate plan forecast and on possible proceeds from litigation (paragraphs 2.44 to 2.45). The Department did not include a provision for a clawback on any capital gains in the event of the company being sold within a given period after privatisation. The Department’s view is that the company’s worth lies in their intellectual property portfolio, the future value of which would be received through clawback on income, and that the Secretary of State’s special share restricts the possibility of a sale for up to five years from the sale (paragraphs 2.46 to 2.47).

14 Having regard to the sale objectives, the Department’s financial advisers recommended the bid from the Anglo-American consortium (paragraphs 2.48 to 2.50).

15 On sale proceeds, the Department concluded that the Anglo-American consortium were in the lead (paragraph 2.51). As regards the continuation of the company’s technology transfer activities, the Department found the bids to be finely balanced. They and their advisers had no reason to doubt that both consortia would seek to maintain the company’s independence, integrity and impartiality. They concluded however that, while the longer term was uncertain, sale to the management-led consortium would enable the company to adjust to life in the private sector, and to demonstrate their independence and viability, even though this meant accepting lower proceeds. The Department also concluded that it was appropriate to give preference to the management-led consortium on the grounds of the greater involvement in the business of the management and employees, and because they believed the consortium offered the better prospect of continuing the company’s service to both universities and United Kingdom companies (paragraphs 2.52 to 2.57).

16 In the negotiations leading to the completion of the sale, the management-led consortium sought a contribution of £650,000 towards their costs which the Department refused. The Department accepted the consortium’s revised bid of £14.25 million. Agreement was reached on initial proceeds of £27.75 million, compared with the consortium’s final competitive bid of £28.3 million. These proceeds were subject to adjustment, up or down, in the light
of the company's aggregate cash and net current liabilities at the date of sale and a requirement that cash should amount to at least £2 million. Audited completion accounts giving this information were under negotiation between the Department and the consortium for a year, during which the difference between the two sides was narrowed. However, each side had different views on the treatment of particular items. On 30 March 1993 both sides formally agreed a nil settlement. The Department believed that they were unlikely to secure further concessions from the consortium without incurring disproportionate costs, and that the uncertainties involved in using an independent expert to determine the settlement risked ending up with a worse outcome. The initial sale proceeds therefore remained at £27.75 million (paragraphs 2.61 and 2.65).

Conclusion

17 The Department's financial advisers succeeded in stimulating competitive bidding for a highly specialised company, in competing for which investors were required to form consortia. Given the commercial sensitivity of the company's business, and the uncertainty over income projections, it was perhaps inevitable that there would be differing views between the Department, the company and the competing consortia about the nature and amount of the information that should be provided to the consortia. Nevertheless, the Department arranged for as much information as possible to be made available to the bidding consortia. Although it was inevitable that the company's management would have a fuller knowledge of the company's activities, the non-executive directors and the Department took reasonable steps to ensure that members of the management-led consortium were not given privileged access to information about the company.

18 In spite of these problems, two of the three consortia who did not include the company's management among their members proceeded to the formal bidding stage. One of these went forward to the final competitive bidding stage, producing a higher bid (£30.4 million) than that of the management-led consortium (£28.3 million). In choosing to sell the company to the lower bidder, the Department were putting a price (£2.1 million) on their judgement that selling the company to the management-led consortium would give it a better opportunity to survive as an independent and viable organisation. By the time the sale was completed, for initial proceeds of £27.75 million, that price had risen to £2.65 million. This is equivalent to a discount to the higher bid of 8.7 per cent.

19 The Department's acceptance of a nil payment either way in settlement of the completion accounts resulted in no increase in the sale proceeds, but avoided the additional costs of using an independent expert to settle the matter, which might have outweighed the benefits, and a possible payment to the consortium.

20 The scope for maximising proceeds was inevitably reduced by the safeguards introduced by the Department to protect the continuity of the business, but it is not possible to determine the impact. The £15 million to £30 million range of the Department's valuation of the company took into account the various constraints on the possible structure of any bids and the way in which the business might be conducted in the future.
v) Control of costs

21 The National Audit Office examined whether the Department had

- selected advisers on a competitive basis; and
- established sound budgetary and financial controls.

22 All the Department's principal advisers were chosen on the basis of
competitive tendering. The Department regularly revised their forecast of
costs and in September 1991 produced a forecast of £2.32 million as a
reasonable benchmark. In the outturn, the costs amounted to £2.92 million.
The main components of the additional expenditure of £0.6 million were
payment of fees in excess of the contracts and payments for additional work
not provided for in the September 1991 forecast, but which the Department
considered necessary for the satisfactory completion of the sale (paragraphs
3.5 to 3.7).

23 The Department set up controls over the company's cash and working
capital in the final weeks of the sale. They required the company to seek
their approval before making payments over £100,000 and monitored the
company's cash position.

Conclusion

24 Although the Department regularly revised their forecasts, it would not have
been possible to foresee all the work that was necessary to complete this
complex sale satisfactorily. They commissioned additional work where it
appeared to be prudent to do so, and kept their advisers under control
despite the hectic pace of events. The additional payments of fees in excess
of contracts to some advisers were reasonable in the light of the additional
effort required. The Department's controls over the company's cash and
working capital were sound and effective.
Part 1: The company and the sale

1.1 On 31 March 1992 the Department of Trade and Industry (the Department) sold British Technology Group (the company) for initial proceeds of £27.75 million to a consortium of investors. The consortium, which included an employee share trust, financial institutions and UK universities, were led by CIN Venture Managers Ltd, a venture capital company, and the company’s management and employees (the management-led consortium). The sale followed competitive bidding involving a number of consortia. The initial proceeds to the Department (Table 1) consisted of a payment from the consortium of £14.25 million in consideration of the sale and payments of £13.5 million from the cash reserves of the company. The net assets of the company acquired by the consortium at the completion of the sale included £4.3 million cash.

Table 1: Initial proceeds

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<thead>
<tr>
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<th>£ million</th>
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<tbody>
<tr>
<td>Initial payment</td>
<td>14.25</td>
</tr>
<tr>
<td>Payments from company's cash reserves</td>
<td>13.50</td>
</tr>
<tr>
<td>Total</td>
<td>27.75</td>
</tr>
</tbody>
</table>

Source: The Department of Trade and Industry

This Table shows the initial proceeds to the Department of Trade and Industry from the sale.

1.2 The payment of £14.25 million was subject to adjustment, up or down, in the light of the actual cash and net current liabilities of the company at the date of sale. The Department and the management-led consortium were unable to agree the audited completion accounts which presented this information and on 30 March 1993 settled for making no adjustment. The initial proceeds therefore remained at £27.75 million (paragraphs 2.62 to 2.65). Additional proceeds may, however, arise over the five years to 31 March 1997 from clawback on net revenues in excess of those forecast in the company’s 1991 Business Plan and on the proceeds of the sale of land and buildings (paragraphs 2.20 to 2.22).

The company

1.3 The company are engaged in technology transfer, that is the commercial exploitation of inventions and new processes. The work involves:

- identifying, developing and protecting commercially viable technology arising from research carried out by individuals, universities and other research organisations (the inventive sources);
- licensing the resulting intellectual property rights to companies throughout the world and sharing the resulting income with the inventive sources;
- assessing the commercial potential of companies’ own technology and licensing this technology to other companies worldwide; and
- investing in companies developing new products.

1.4 The company deal with a wide range of technologies. Most inventions fail, but the experience of the company and their predecessors over 40 years has been that a small number of technologies have produced significant returns (Table 2).

Table 2: Estimated expenditure and revenue 1949–1991

<table>
<thead>
<tr>
<th></th>
<th>£ million</th>
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<tbody>
<tr>
<td>Total Expenditure</td>
<td></td>
</tr>
<tr>
<td>Cephalosporin (an antibiotic)</td>
<td>0.9</td>
</tr>
<tr>
<td>Pyrethin (an insecticide)</td>
<td>4.2</td>
</tr>
<tr>
<td>Magnetic resonance imaging (an alternative to x-rays)</td>
<td>0.8</td>
</tr>
<tr>
<td>All other technologies and investments</td>
<td>5.3</td>
</tr>
<tr>
<td>Total expenditure and revenue since 1949</td>
<td>208.7</td>
</tr>
</tbody>
</table>

Source: Sale information memorandum

Note: The figures are not expressed at constant prices.

This Table shows that gross revenue from three technologies exceeded total expenditure since the establishment of the National Research Development Corporation, the company’s forerunner, in 1949.
1.5 Revenues from the antibiotic cephalosporin ceased in 1987 and those from the insecticide pyrethrin will end in March 1995. Revenues from magnetic resonance imaging, an alternative to x-rays, are expected to continue until the end of the century. Appendix 1 gives more information about the business.

**The sale**

1.6 The Government decided to privatise the company on the grounds that they were already operating on a commercial basis in an increasingly competitive international market place. The Department’s objectives for the sale were:

- to maximise the net return to the taxpayer consistent with a good prospect of the continuation of the company’s technology transfer activities.

**Scope of the National Audit Office examination**

1.7 The National Audit Office examined:

(a) how far the Department had achieved the sale objectives (Part 2 of the report); and

(b) how the Department controlled the costs of the sale (Part 3 of the report).

1.8 This work included examination of Departmental papers and discussions with Departmental officials and their advisers. The National Audit Office compared the actions taken by the Department with recent recommendations made by the Committee of Public Accounts arising out of the handling of earlier sales. A summary of the main findings is at Appendix 2. The National Audit Office consulted senior management of the company and members of the various consortia which submitted bids in the sale. The National Audit Office obtained advice from Ernst and Young Corporate Finance. The National Audit Office are grateful for the assistance they received in carrying out this study and producing their report.
Part 2: Achievement of objectives

2.1 This part of the report examines how far the Department were successful in achieving the sale objectives to maximise the net return to the taxpayer consistent with a good prospect of the continuation of the company's technology transfer activities.

2.2 The Government were particularly concerned to find buyers who would take a long term view, and not seek to break up the company or otherwise threaten the continuation of the company's existing business. They judged that the continuation of the business could be put at risk if a single buyer was able to purchase the company outright or to achieve a controlling interest. For example, if the company were to be acquired by an industrial concern with an interest in the success or failure of a particular area of technology, this might result in the suppression of technologies in competition with that industrial concern's own commercial interests. This could prejudice the company's reputation for independence and integrity with their other clients. The Government therefore decided to seek bids from groups of investors (consortia) rather than from single buyers.

2.3 In addition, the Government decided to introduce safeguards into the terms on which the company would be sold. These included provision for the Secretary of State for Trade and Industry (the Secretary of State) to hold a special share for up to five years to enable the company to adjust to life in the private sector. This special share would require the Secretary of State's approval for the disposal of the whole or a material part (25 per cent) of the assets or business of the company, and for any amendment to a restriction on any organisation owning or controlling more than 15 per cent of the voting rights in the company. The 15 per cent limit is to continue after the five year period, and may only be changed with the agreement of members exercising 75 per cent of the voting rights.

2.4 The primary purpose of the 15 per cent limit was to preserve the company's independence from outside interference. The Government stated that they were prepared to consider higher individual shareholdings, within the context of a consortium, should this prove necessary to attract the right bidder, but that they would not consider individual shareholdings high enough to permit one party to achieve control of the company. The draft Articles of Association laid before Parliament excluded an employee share ownership trust from this 15 per cent limit.

2.5 Through the draft Articles of Association, the Government also provided for the Committee of Vice-Chancellors and Principals to appoint one director of the company, and for another director to be appointed for his experience of, amongst other things, the development or exploitation of public sector research.

2.6 The Government gave assurances to Parliament to this effect, and these requirements were stated in the Information Memorandum sent to potential bidders in November 1991.

2.7 The National Audit Office examined whether, in pursuit of their objectives and these requirements, the Department had:

- identified the most appropriate method of sale;
- valued the business by reference to the most appropriate criteria;
- considered ways in which a proportion of any value not identified at the time of the sale might subsequently be recovered through suitable clawback provisions; and
- negotiated the sale on the best possible terms for the taxpayer, including seeking competitive bids and securing reasonable and equal access to information for bidders.

Method of sale

2.8 Before the Government's decision to seek consortium bids for the company, the Department had asked their financial advisers, Price Waterhouse, to assess the most
appropriate method of privatising the company in the light of the sale objectives. Price Waterhouse identified five options.

i) Public flotation

2.9 This option had the advantages of offering a reasonably broad shareholder base, a ready market for the company's shares and increased public awareness about the company. The disadvantages were that the company's specialised activities, coupled with a declining performance and unpredictable environment, meant that the sale would not have a wide appeal; short-term stock market pressures to preserve the share price would not allow the company to manage its business on a long-term basis; and the costs of this route, assuming the offer was underwritten, were likely to be higher than other privatisation options. Price Waterhouse concluded that flotation was unlikely to be the right route.

ii) Private placing with long-term equity investors

2.10 This option would involve inviting long-term equity investors to take minority stakes in the business. If suitable investors were prepared to take a long-term view, the continuation of the business should be achievable. Another advantage was that the Department could choose which investors to approach. Price Waterhouse were concerned that this option might lead to a low sale price because of caution on the part of equity investors. On balance, however, they regarded a private placing as offering a viable route.

iii) Management buyout

2.11 The nature of the company's business was judged by Price Waterhouse to be unsuited to the traditional method of financing a management buyout: debt finance would be difficult to raise against the company's assets and difficult to service given the uncertain nature of the company's cash flows. Price Waterhouse considered, however, that it might be in the Government's interest to encourage management to be involved in the sale, but not in a way which would deter other potential bidders.

iv) Sale to a charitable trust

2.12 This option would involve a charitable trust or foundation owning all or part of the business. Although they felt that the company's continuity could probably have been secured by this route, Price Waterhouse concluded that this option was unlikely to maximise sale proceeds, on the grounds that a trust might not be able to raise sufficient funds.

v) A trade sale

2.13 Price Waterhouse believed that a trade sale to a consortium of investors could introduce competition into the sale process, while potentially securing the continuation of the company's activities. The disadvantages of the consortium approach were that competition would depend on how many consortia were formed; in addition, commercial confidentiality might be put at risk because of the number of parties involved; and the sale might take longer to complete than to a single trade buyer. In Price Waterhouse's view, however, the consortium approach represented a viable form of trade sale.

The Department's decision

2.14 Price Waterhouse concluded that sale by way of a private placing or to a consortium of trade purchasers appeared to be feasible routes. The Department judged that the private placement route would only provide effective competition if the demand for shares significantly exceeded supply, but they were not convinced that there would be a sufficient number of interested investors. By contrast, they saw a good prospect of maximising competition through consortia, especially by encouraging rival bids from two or more consortia. They therefore chose the consortium approach.

Valuing the business

2.15 In December 1991 the Department asked Price Waterhouse to update the valuation of the company they had carried out earlier that year. The purpose was to provide a benchmark to assist the Department in assessing the comparative merits and adequacy of bids received from prospective purchasers of the company.

2.10 Valuation was difficult because the timing and amount of future income streams were uncertain, and because there were no companies trading in the United Kingdom
private sector with which the company could be directly compared. Price Waterhouse took the view that the amount a consortium would be prepared to pay for the company as a going concern would depend upon the future net income likely to be generated, and the level of risk that might be attached to such income. They concluded that the most appropriate method of valuation was discounted cash flow. The cash flow projections used for the valuation were derived from the company’s 1991 ten year corporate plan, supplemented by additional financial information produced by the Department’s reporting accountants.

2.17 As at 3 January 1992, Price Waterhouse valued the company at a range of £15 million to £30 million. The valuation covered a number of scenarios, for example, that the business could be run in accordance with the corporate plan or that it could be run down in an orderly fashion over the 10 year corporate plan period. The valuation assumed that the Department would receive £13.5 million from the cash reserves of the company and leave £10 million cash in the business. Price Waterhouse stated that, to the extent that the cash balance on sale was less than £10 million, there would be a corresponding decrease in their valuation range on a £1 for £1 basis. The valuation also took into account the various constraints set out in the Information Memorandum, relating to the possible structure of bids for the company and the way in which the business might be conducted in the future.

2.18 The Department subsequently commissioned PA Consulting Group to examine the company’s income projections in relation to their portfolio of intellectual property assets, and to provide an independent assessment of the company’s likely future income. PA Consulting Group’s assessment was broadly in line with the company’s projections.

Valuation: property assets

2.19 The Department commissioned a valuation of the buildings owned by the company at 99-101, Newington Causeway, London SE1. This resulted in an open market valuation of £4.1 million as at 1 August 1991. In view of the general decline in property values, the Department subsequently obtained a second valuation. This resulted in a reduced open market valuation of £3.6 million, as at 28 February 1992.

Clawback

2.20 The Department considered with their lead financial advisers the case for introducing clawback provisions to enable the taxpayer to benefit from any value not identified at the time of the sale. The two areas examined for clawback were, first, land and buildings and, second, the intellectual property rights which form the main source of the company’s income.

2.21 The Information Memorandum informed potential investors that the sale arrangements would make provision for the Government to be entitled to further consideration in the event of any gain from the sale of the company’s land and buildings within five years after privatisation. The clawback provision subsequently agreed with the purchaser entitles the Department to 50 per cent of gains after tax over the value at 28 February 1992 arising during the five year period to 31 March 2007.

2.22 The Information Memorandum also stated that the Government were concerned to ensure that they received due benefit from income arising from the company’s existing portfolio of technologies to the extent that this exceeded the amounts projected by the company in their corporate plan. In structuring their initial bids, prospective investors were invited to indicate how they would address such a situation.

Negotiating the sale: obtaining indicative bids

2.23 Price Waterhouse met some 30 organisations who had expressed interest in the sale, and sent details to a further 50 or so potential investors in the United Kingdom. Price Waterhouse also identified and sent briefing material to 62 companies in the United States and 90 companies in Europe. Copies of the Information Memorandum inviting initial bids were sent to 80 organisations who had expressed an interest in the sale. In addition, an advertisement was placed in the financial press. Prospective investors were invited to submit their preliminary proposals, including
indicative bids and consortia details, to the Department by 6 January 1992. Appendix 3 sets out the timetable and key stages in the sale.

2.24 The company's senior management told the Department at the end of November 1991 that they were considering the feasibility of organising a consortium involving management and employees to bid for the company. The Department considered the arguments for and against allowing the management to do so. On the one hand, they were concerned about the potential conflicts of interest which could work against other prospective purchasers getting the information they needed to compete on equal terms. They also wished to ensure that the business was managed in an objective manner in the period leading up to the sale. On the other hand, they saw advantage in allowing the management and employees to participate in the bidding, on the grounds that the increased competition might help to maximise sale proceeds and to maintain the commitment of management and staff during the sale process.

2.25 The Department decided to allow management and employees to participate in the bidding process, on the understanding that any consortium involving management and employees would compete on equal terms with other consortia, and should be seen to do so. The company's management publicly declared their intention to form a consortium in December 1991, by which time three other consortia had decided to submit indicative bids.

2.26 The four consortia submitting indicative bids are set out in Table 3, together with the bids. These were submitted against the background of the Department's intention, stated in the Information Memorandum, of leaving approximately £10 million in cash in the company at the time of the sale, while taking some £12 million plus cash and short term deposits relating to funds provided for the company's predecessors in earlier years (Appendix 1).

<table>
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<tr>
<th>Table 3: Comparison of indicative bids</th>
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<tr>
<td>Consortium</td>
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<tr>
<td>The management-led consortium;</td>
</tr>
<tr>
<td>The Anglo-American consortium, led by Research Corporation Technologies of Tucson, Arizona;</td>
</tr>
<tr>
<td>The Technology Marketing Corporation Ltd consortium, led by Strategy International; and</td>
</tr>
<tr>
<td>The Mason/Finlay Bank consortium, led by Sir Ronald Mason and James Finlay Bank</td>
</tr>
</tbody>
</table>

Source: Price Waterhouse

This Table shows the four consortia submitting indicative bids and the amount of each bid.

2.27 The payments proposed in these indicative bids came within Price Waterhouse's valuation range of £15 million to £30 million, with three towards the upper end of that range. Price Waterhouse recommended that all four consortia should be invited to submit formal bids. The Department accepted this advice and the four consortia indicated that they wished to proceed to the formal bidding stage.

Negotiating the sale: obtaining formal bids

2.28 The Department decided to permit the four consortia equal access to selected information about the company, in carefully controlled circumstances, to assist them in drawing up their formal bids. The Department were concerned to guard against the management-led consortium having greater access to information than the other bidders. But they were also concerned to respect the confidentiality and sensitivity of certain categories of data, in particular licence terms, bearing in mind that the other bidders were actual or potential competitors of the company. The company also made representations to the Department that licence terms were confidential due to the understandings reached between the company and the other parties to the licence agreements.

2.29 The Department introduced the following rules and procedures, which were addressed to these concerns:

- a Price Waterhouse representative or a non-executive director of the company would attend all meetings between the
company's management and their consortium partners or the consortium's advisers;

- all written information on the company distributed to the members of the management-led consortium would be routed through Price Waterhouse and made available to the other bidders;
- the City Code on Takeovers and Mergers would apply to the sale: under this Code, the company's financial advisers were required to disclose to the Department and Price Waterhouse any price and commercially sensitive information released by management to their consortium partners; and
- all potential investors were required to sign confidentiality undertakings.

2.30 The Department valued the important role of the company's non-executive directors in providing independent and impartial advice and in ensuring that fairness was maintained.

2.31 Data rooms were set up at Price Waterhouse's London offices and at the company's London headquarters. The data room at Price Waterhouse contained financial information about the company's recent performance and future prospects (including profit projections), details of freehold and leasehold properties, and summary information on the company's principal technologies. Section A of Appendix 4 to this report sets out the principal categories of information held in this room.

2.32 The data room at the company's offices was set up to provide access to detailed information about licences, agreements and patents, but without royalty rates and financial information (Section B of Appendix 4). Price Waterhouse told bidders that certain unspecified documents might be made available at the final stage to the successful bidder.

2.33 Prospective investors were required to follow strict procedures in using the data rooms. Entry was restricted to those named in the confidentiality undertaking signed by each prospective investor. Writing materials were permitted inside the rooms but not dictating machines, computers, cameras, photocopiers or fax machines. Telephone calls could be made only outside the rooms and no documents could be removed. No photocopies were permitted, although Price Waterhouse provided copies of pre-selected documents on request. Any questions about the data had to be submitted in writing by the leader of each consortium.

2.34 All four consortia requested additional information, but the Anglo-American consortium and the Mason/Pinlay Bank consortium complained to Price Waterhouse that the information initially provided in the data rooms was insufficient to enable them to submit formal bids. They sought more detailed information, for example about the financial arrangements provided for in individual agreements. Section C of Appendix 4 to this report shows the information requested by each consortium.

2.35 The company's Board—including its non-executive directors—represented to Price Waterhouse, however, that it could be commercially damaging to give the consortia access to certain detailed information, for example on corporate strategy and income flows from specific intellectual property rights and licences. Some of the company's agreements with licensees were drawn up in terms of absolute confidentiality. Other agreements contained information about licensees, or about the company's appraisals of various technologies, which was commercially sensitive. In addition, part of the company's expertise lay in the detailed drafting of patents and licence agreements. The company were particularly concerned that the company's competitive position could be prejudiced if such information was released to potential competitors, even though all investors had signed confidentiality undertakings.

2.36 Although legal advice sought by the company suggested that there were grounds for not allowing access to licence agreements, the Department arranged for as much information as possible to be made available to bidders. Arrangements were put in place for bidders to examine the legal validity of licence agreements and bidders were allowed to talk to the company's divisional heads and the Department's reporting accountants. The two consortia which the Department invited to proceed to the final competitive bidding stage were subsequently given access to the revenue projections for certain key technologies (paragraph 2.43 and Section C of Appendix 4).
2.37 The Anglo-American consortium pressed for details of licence agreements and projections of future revenue, on a year by year basis, for a number of technologies, on the grounds that they needed this information to make a formal bid. The lead member of this consortium, Research Corporation Technologies, offered in return full reciprocity of information on all their licences. The Board of the company, who regarded Research Corporation Technologies as their principal competitor, declined this offer, and in the light of this refusal the Department and their financial advisers could take it no further.

2.38 On 15 February 1992, the financial advisers made available to consortia a summary statement of the company's net current asset position at 31 December 1991. Sections B and C of Appendix 4 give more details of the additional information requested, how much of this was supplied, and at what stages, and what was withheld.

2.39 The Mason/Finlay Bank consortium withdrew on 18 February 1992 without submitting a second bid, commenting that the withholding of key information on the company had made it impossible, within the timescale, to communicate sufficient information to investors to enable them to take a firm decision on joining the consortium. Price Waterhouse disagreed that insufficient information had been provided, noting that the three other consortia were still in the running.

2.40 The three remaining consortia submitted formal bids by the deadline of 19 February 1992. By this time the Department had confirmed to the bidders that the sum they intended to withdraw from the cash reserves of the business was £13.5 million. In their bids, the consortia set out their requirements for the amount of working capital including cash they wished to have in the business at the time of the sale. Among other aspects dealt with in the bids were their intentions as regards running the business, and their proposals on clawback. In each case the payment proposed was substantially below the indicative bid. In their bid, the Technology Marketing Corporation consortium sought a cash payment from the Department, having regard to their intention to restructure the business. Details of the three bids are set out in Table 4.

2.41 Price Waterhouse evaluated each bid against a range of criteria including:
- the nature of each consortium (including the number of investors and proportion of equity to be held by each party);
- how each bid would be financed;
- each consortium’s plans for the future of the business up to and beyond five years;
- how management and employees would be involved in the privatisation; and
- the likely sale proceeds from each bid, including potential clawback income.

2.42 Price Waterhouse concluded that each bid had merits. The Anglo-American consortium offered the highest initial payment. The management-led consortium and the Technology Marketing Corporation consortium offered the widest spread of ownership. A strength of the management-led consortium’s bid lay in management’s knowledge of the company’s business. Although all three bids made provision for employee participation in the sale, the management-led consortium offered the most comprehensive plans, which included a proposed employee share scheme. All the consortia intended to continue the activities of the business.

2.43 Having regard to the criteria for evaluating these bids (paragraph 2.41) the Department decided to invite the management-led consortium and the Anglo-American consortium to proceed to the final competitive bidding stage.
Negotiating the sale: final competitive bids

2.44 The management-led consortium and the Anglo-American consortium each submitted final bids by the 27 February 1992 deadline set by the Department. By this time, it had become clear to the Department, from information also made available to the consortia, that the amount of cash which would be left in the company at the time of the sale was unlikely to amount to more than £2.5 million, compared with the Information Memorandum figure of £10 million. Table 5 sets out the bids submitted by the two consortia. Allowing for the reduction of £7.5 million in the estimate of the amount of cash to be left in the company, payments proposed were at about the mid point of Price Waterhouse's valuation range. The management-led consortium separately requested up to £1 million to cover the consortium's privatisation costs.

<table>
<thead>
<tr>
<th>Table 5: Comparison of final competitive bids</th>
</tr>
</thead>
<tbody>
<tr>
<td>Management-Led Consortium</td>
</tr>
<tr>
<td>Initial payment (£ million)</td>
</tr>
<tr>
<td>Payments from company's cash reserves (£ million)</td>
</tr>
<tr>
<td>Total (£ million)</td>
</tr>
</tbody>
</table>

Source: Price Waterhouse

This Table shows each consortium's final competitive bid. After being selected as the preferred purchaser, the management-led consortium reduced their bid by £0.5 million to £27.75 million which the Department accepted (paragraph 2.61).

2.45 Each bid contained revised proposals for clawback on income in excess of the corporate plan forecast, and possible proceeds from litigation in progress at the date of sale. These clawback proposals are compared in Table 6. The most likely clawback to arise will be in relation to litigation, in respect of which the Department would recover the full amount under the Anglo-American consortium's proposals. By contrast, the management-led consortium proposed that any clawback on litigation proceeds would be limited to 60 per cent, after aggregation with clawback on income, which could be a negative amount.

2.46 The Department and their lead financial advisers did not ask the consortia to make proposals for a clawback on any capital gains in the event of the company being sold within a given period after privatisation. In the sale of National Transcommunication Limited, on which I have separately reported (HC 285 of Session 1992–93), the Home Office negotiated post flotation clawback terms with the purchaser. Price Waterhouse were also lead financial advisers for that sale.

2.47 The Department told the National Audit Office that the restrictions on sale during the five years that the Secretary of State's special share was likely to be held, and the poor prospects of flotation, did not warrant the introduction of clawback on capital gains. The valuation of the company also confirmed that their worth lay essentially in intellectual property holdings for which the Department would receive value in the initial sale proceeds. To the extent that performance might exceed expectations, future value would be received through clawback on income. Any increase in the value of land and buildings would also be recovered through other clawback arrangements.

Negotiating the sale: appraisal of bids

2.48 Following discussions with each consortium to clarify certain aspects of the bids, Price

<table>
<thead>
<tr>
<th>Table 6: Comparison of clawback proposals on income and litigation proceeds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Clawback</td>
</tr>
<tr>
<td>Intellectual property covered</td>
</tr>
<tr>
<td>Period to which clawback relates</td>
</tr>
<tr>
<td>Proportion of income over forecast to be paid to Department</td>
</tr>
<tr>
<td>Nature and timing of payment</td>
</tr>
<tr>
<td>Litigation proceeds to be paid to Department</td>
</tr>
</tbody>
</table>

Source: Price Waterhouse

This Table compares the clawback proposals contained in each consortium's final competitive bid.
Waterhouse wrote to the Department on 27 February 1992 advising that, given the Department’s objectives of maximising proceeds consistent with ensuring continuity of the business, the better bid, in their opinion, was that of the Anglo-American consortium.

On sale proceeds, they noted that the Anglo-American consortium’s bid amounted to £30.4 million, compared with £28.3 million from the management-led consortium (Table 5). In addition, the Anglo-American consortium were offering the Department the whole net proceeds from the company’s major outstanding litigation case, and a year by year clawback on intellectual property rights above plan for nine years on all technologies. The management-led consortium offered clawback over five years net of shortfalls, and the proceeds from litigation were to be included in that calculation (Table 6).

On continuity of the business, Price Waterhouse noted that all the members of the Anglo-American consortium were prepared to give a five year commitment, whereas the management-led consortium were not. As far as the longer term was concerned, although the lead member of the Anglo-American consortium, Research Corporation Technologies, might gain control of the company, Price Waterhouse noted that they were a trust whose deeds required them to devote their efforts solely to technology transfer. By contrast, the management-led consortium bid was silent about what would happen after five years. In Price Waterhouse’s view, there was a possibility that some of the members would seek to leave the management-led consortium after five years; and Price Waterhouse could not judge the consequences of this for the continuity of the business.

Maximising sale proceeds

The Department noted that, leaving aside the request from the management-led consortium for a contribution towards costs, the difference between the two bids was £2.1 million, plus the prospect of higher litigation proceeds, in favour of the Anglo-American consortium. They concluded that, on sale proceeds, the Anglo-American consortium were in the lead.

Continuation of the business

The Department noted that both consortia contained blocks of shareholdings in excess of the 15 per cent limit set by the Government (paragraph 2.3). In the case of the management-led consortium, however, this comprised 26 per cent of voting rights for an employee share ownership trust—an arrangement which was specifically excluded from the 15 per cent limit (paragraph 2.4). In addition, about 8 per cent of the equity would be reserved for individual managers and employees. In the Anglo-American consortium, Research Corporation Technologies would hold 20 per cent of the voting rights and, given the way the bid was structured, there was a strong probability, though not a certainty, that Research Corporation Technologies would take control of the company after five years. The Anglo-American consortium had also declared a willingness to introduce an employee share ownership trust, with up to 15 per cent of the voting rights.

As regards the continuation of the company’s technology transfer activities, the Department found the bids to be finely balanced. They and their advisers had no reason to doubt that both consortia would seek to maintain the company’s independence, integrity and impartiality. The Department believed that the management-led consortium would continue to broaden the base of the business, in which an increasing proportion consisted of licensing the intellectual property rights of companies to other companies. The Anglo-American consortium were seen as more likely to be helpful if the development of the intellectual property rights of universities was regarded as more important than technology broking between companies, since the former was the main area of activity of Research Corporation Technologies.

The Department recognised that it was unclear, looking beyond the five year currency of the Government’s special share, whether either consortium would continue or whether the company might be acquired by another owner or owners. The purpose of the initial five year period however was to enable the company to adjust to life in the private sector, and to demonstrate their viability. The Department had to make a judgement on the probabilities. They concluded that, while the longer term was uncertain, sale to the
management-led consortium would enable this option to develop. By contrast, if the company were sold to the Anglo-American consortium, that option would be foreclosed, and the structure of the bid indicated the probability of Research Corporation Technologies acquiring control after five years. From that point of view, sale to the Anglo-American consortium could be seen as a deferred trade sale to a single buyer, contrary to the assurances given to Parliament (paragraphs 2.2 to 2.4).

2.55 The Department told the National Audit Office that giving the company a chance to survive as an independent and viable organisation was the overriding consideration which led the Secretary of State to conclude that exclusive negotiations should be conducted with the management-led consortium, even though this meant accepting lower proceeds.

2.56 The Department identified the following secondary considerations in favour of the management-led consortium’s bid:

(a) It was appropriate to give preference to the management-led consortium on the grounds that this consortium gave greater involvement to the company’s management and employees, since they would have a continuing interest in the business; and

(b) The Department’s intention was to sell the company to a consortium which would independently continue the technology transfer and other existing activities in the longer term. The Department believed that the management-led consortium offered the better prospect of continuing the company’s service to both universities and United Kingdom companies because they involved the existing management and employees in implementing the objectives of the business.

2.57 The Department accordingly announced on 11 March 1992 that the management-led consortium had been selected as the preferred purchaser.

2.58 Research Corporation Technologies told the National Audit Office that, as well as submitting the higher bid, they believed their bid offered the better guarantee for the continuation of the company’s business. They regarded their operations as complementary to those of the company: few if any of the technologies of each organisation were in direct competition with each other. In their view, the two organisations would together have formed a potent portfolio of technologies, acting as a magnet to inventive sources.

2.59 Research Corporation Technologies would have preferred to buy the company outright, but it would have been their intention to maintain the company as a separate entity. They had concluded that the Department were not concerned about ownership after the expiry of the initial five year period. In August 1991 the Department’s legal advisers told the consortium’s solicitors that 15 per cent would be the benchmark level of shareholding. The purpose of the limit was, amongst other things, to provide some protection against the company being captive to one shareholder, but there was some flexibility between 15 per cent and the 50 per cent level that Research Corporation Technologies preferred. Subsequently, the Department’s financial advisers indicated that around 30 per cent might be acceptable. Finally, just before the final bids had to be submitted, the consortium were advised by the Department that their shareholding ought not to exceed 20 per cent.

2.60 Research Corporation Technologies told the National Audit Office that to reduce their holding of voting shares below 20 per cent would have increased the costs of servicing the capital, and would have reduced their bid to the point where they believed it might no longer have been competitive. They told the National Audit Office that their commitment to the company would have been long term, as evidenced in the low rate of return on their investment which they had assumed for the first five years, and that they had been intending to continue with those parts of the company’s existing business which they judged to be commercially viable.

Negotiating the sale: completion

2.61 The management-led consortium sought a contribution of £550,000 from the Department towards the costs they had incurred in putting together their bid. The Department refused, in line with Treasury guidelines that there should be no public support for such a bid if it was successful. Following negotiation, the
management agreed to buy a copy of the company's income assessment by PA Consulting Group for £100,000. The consortium subsequently reduced their bid by £550,000 to £14.25 million which the Department accepted. Agreement was therefore reached on proceeds of £27.75 million, by comparison with the consortium's previous bid of £28.3 million.

2.62 These proceeds were subject to adjustment. The agreement between the Department and the management-led consortium stipulated that the final sale proceeds were dependent on the aggregate of cash and net current liabilities left in the business at the date of the sale (31 March 1992), and that cash should amount to at least £2 million. The Department were to repay to the consortium any amount by which the aggregate of cash and net current liabilities at that date was less than £100,000. In addition, if the aggregate of any such repayment and the cash was less than £2 million, the Department were to pay the difference to the consortium. If, however, the aggregate of cash and net current liabilities exceeded £100,000, the consortium were to pay the excess to the Department, to the extent that this did not reduce the cash balance at the date of sale below £2 million.

2.63 Audited completion accounts giving this information were submitted by the consortium in May 1992. The accounts suggested that the Department should make a payment of £1.2 million to the company. The Department formally objected to the accounts and appointed Coopers and Lybrand to review them. Amendments proposed by Coopers and Lybrand in July 1992 suggested that the company should pay the Department £1.05 million.

2.64 The Sale Agreement made provision for the matter to be settled by an independent expert agreed by both sides if they could not reach a negotiated settlement. Subsequent negotiations narrowed the difference between the two sides but failed to resolve the treatment of particular items. Both sides acknowledged that a nil payment either way would be acceptable. On 30 March 1993, a year after the sale, the Department and the consortium formally acknowledged that they had been unable to agree the completion accounts and agreed on a nil payment either way. This was in line with Price Waterhouse's advice that such an outcome must be close to the maximum likely and that to secure further ground was likely to require arbitration and with it the real risk of finishing up with less rather than more. The initial sale proceeds therefore remained at £27.75 million.

2.65 The Department accepted a nil settlement because they recognised that, after a prolonged period of discussions during which they had not resolved all of their differences with the consortium, they were unlikely to secure further concessions from the consortium without incurring disproportionate costs, and because recourse to an independent expert carried the risk of ending up with less rather than more due to the uncertainties involved. In addition, the Department saw merit in avoiding the further costs of using their own advisers and the additional costs of employing the independent expert. The Department told the National Audit Office that although they failed to increase the initial sale proceeds, they avoided a potential payment of £1.20 million to the consortium as well as the costs of using an independent expert.
Part 3: Control of costs

3.1 The Department estimated the costs of the sale, excluding their own staff costs, to be £2.92 million, or 10.5 per cent of the initial sale proceeds. Table 7 sets out the initial proceeds and costs of the sale.

Table 7: Initial proceeds and costs of the sale

<table>
<thead>
<tr>
<th></th>
<th>£ million</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Sale proceeds:</strong></td>
<td></td>
</tr>
<tr>
<td>Payment by management-led consortium</td>
<td>14.25</td>
</tr>
<tr>
<td>Payment from the company's cash reserves</td>
<td>13.50</td>
</tr>
<tr>
<td><strong>Less costs:</strong></td>
<td></td>
</tr>
<tr>
<td>Advisers</td>
<td>2.80</td>
</tr>
<tr>
<td>Overseas costs</td>
<td>0.08</td>
</tr>
<tr>
<td>Information memorandum</td>
<td>0.03</td>
</tr>
<tr>
<td>Other</td>
<td>0.01</td>
</tr>
<tr>
<td><strong>Net sale proceeds</strong></td>
<td>24.83</td>
</tr>
</tbody>
</table>

Source: The Department of Trade and Industry

This Table shows the initial sale proceeds, costs and net proceeds from the sale of the company.

3.2 The National Audit Office examined whether the Department had:

- selected advisers on the basis of competitive tenders;
- established sound project management and budgetary controls; and
- established appropriate financial controls over the company's assets during the sale period.

Selection of advisers

3.3 The Department chose their principal advisers (Appendix 5) on the basis of competitive tenders. The Department engaged PA Consulting Group on the basis of a single tender in February 1992, to assess the company's intellectual property portfolio (paragraph 2.18). The consultants were engaged after consultations with the Treasury. Alternatives were considered but the Department considered the firm to be well qualified for the task and speed was of the essence.

Project management

3.4 The Department established a steering committee of officials and financial and legal advisers to co-ordinate and direct the sale. A timetable of key tasks was developed and updated from time to time. Not all tasks were foreseen in the original timetable. The budgetary implications are examined below.

Budgetary control

3.5 The Department made a succession of cost forecasts which they regularly revised in the light of unforeseen work that arose from a complex sale. Their first reasonable forecast of outturn, in September 1991, was £2.3 million. In the outturn, the costs amounted to £2.92 million (Table 7). Table 8 sets out the items of additional expenditure, and the underspend, compared with the September 1991 forecast.

Table 8: Comparison of forecast and actual costs

<table>
<thead>
<tr>
<th></th>
<th>£000</th>
<th>£000</th>
</tr>
</thead>
<tbody>
<tr>
<td>September 1991 forecast</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Outturn (see Table 7)</td>
<td>2,319</td>
<td>2,916</td>
</tr>
<tr>
<td>Additional expenditure</td>
<td>597</td>
<td></td>
</tr>
</tbody>
</table>

Explanation of differences

- Additional expenditure under contracts with financial advisers | 178
- Additional expenditure under contracts with reporting accountants | 48
- Lower than forecast expenditure with legal advisers (54)
- Additional items of work not in September 1991 forecast | 425

Total additional expenditure | 597

Source: The Department of Trade and Industry

This Table shows the additional expenditure compared with the September 1991 forecast.

3.6 The Department told the National Audit Office that it could not have been possible to forecast all the additional work that became necessary in handling this complex sale. As for the payments in excess of contract, the Department were satisfied that the high quality of the work necessarily undertaken by
their advisers, and the considerable efforts these advisers made to meet demanding deadlines, justified their decision to meet these extra costs. Generally, the Department were satisfied that they had kept their advisers on a tight rein despite the hectic pace of events. They considered that they had been flexible by taking decisions to commission additional work where it appeared to be prudent to do so, when they could have done nothing.

Control of assets

3.7 Once the management-led consortium were selected as the successful bidder, controls were set up over the company's cash and working capital. The Department required the management to seek their approval for any payments in excess of £100,000 and the Department's reporting accountants monitored the company's cash position prior to the sale. As a result of this monitoring, the Department instructed the company in March 1992 not to make three payments totalling £326,000, on the grounds that these were attributable to the period after the sale. The company considered the payments to be valid, but complied with the instruction.
## Glossary of terms

<table>
<thead>
<tr>
<th>Term</th>
<th>Definition</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corporate plan</td>
<td>The company's 1991 business plan, which contained the management's forecasts of income, expenditure and profits over the ten year period ending 31 March 2001.</td>
</tr>
<tr>
<td>Discounted cash flow</td>
<td>An investment appraisal technique in which estimated future costs and revenues are expressed in terms of their present value.</td>
</tr>
<tr>
<td>Intellectual property</td>
<td>The legal recognition of the ownership of new ideas, giving the proprietor the right to prevent their exploitation by others.</td>
</tr>
<tr>
<td>Intellectual property</td>
<td></td>
</tr>
<tr>
<td>rights</td>
<td></td>
</tr>
<tr>
<td>Invention</td>
<td>A single product, technique or process capable of being protected by patents, copyright or other methods.</td>
</tr>
<tr>
<td>Licence</td>
<td>An agreement allowing a third party use of intellectual property.</td>
</tr>
<tr>
<td>Special share</td>
<td>A share conferring particular rights on the holder.                                                                aversal rights on the holder.</td>
</tr>
<tr>
<td>Technology</td>
<td>A collection of associated inventions which may be protected by some or all of the following: patents, know-how, copyrights, registered and unregistered designs and trade marks.</td>
</tr>
<tr>
<td>Technology transfer</td>
<td>The identification, development, protection and licensing of innovative technology to industry.</td>
</tr>
<tr>
<td>Trade sale</td>
<td>The direct sale of a business in state ownership to another business, or to the management and/or employees of the business being sold.</td>
</tr>
</tbody>
</table>
Appendix 1
The Business

1 British Technology Group were formed in 1981 when the Government merged the operations and management of the National Research Development Corporation and the National Enterprise Board. The National Research Development Corporation were established in 1949 and carried out their work under the provisions of the Development of Inventions Acts, 1948 and 1967. The Corporation’s functions included acquiring, holding or disposing of rights in connection with inventions resulting from public research.

2 The National Enterprise Board were established under the Industry Act 1975. Their functions were to provide finance for industrial investment and to act as a holding company for companies in which the Government had shareholdings. From 1983 the Board’s activities were reduced and, at the time of the sale, their assets comprised a mortgage loan, cash and deposits.

3 Under the Development of Inventions Act, 1948, the National Research Development Corporation had the role of “securing, where the public interest so requires, the development or exploitation of inventions resulting from public research”. Under a Treasury directive issued in 1950 Government departments were required to transfer all their existing and future rights in inventions, with certain exceptions, to the Corporation. The research councils and universities subsequently stipulated that inventions arising out of Government grants or direct funding should also be offered to the Corporation. Around 50 per cent of inventions offered to British Technology Group arose out of this right of first refusal. The rest were communicated to the company for commercial exploitation on an arm’s length basis. In 1985 the Government removed these monopoly rights. At the time of the sale in 1992, the great majority of new inventions offered to the company still came from UK universities and research establishments on arm’s length commercial terms.

4 Although the Corporation and the National Enterprise Board continued to be accountable to Parliament as separate statutory entities, they operated jointly under the trade name British Technology Group until 5 January 1992. On 6 January 1992, under section 1 of the British Technology Group Act 1991, the assets and liabilities of the Group were transferred to a newly incorporated company, British Technology Group plc, which subsequently re-registered as British Technology Group Ltd.

5 The business has three principal characteristics:
   - long term—the lead time from the development of an invention to revenue earning can be many years;
   - high commercial risk—the majority of technologies generate low returns or none;
   - some technologies however have the potential to generate very high rewards.

6 At the time of the sale (31 March 1992), there were four operating divisions: Science, Pharmaceuticals, Engineering, and Electronics and Information Technology. The Group had two operating subsidiaries, BTG USA, based in Philadelphia, and British Technology Group Inter-Corporate Licensing Ltd, both of which aim to commercialise developed technologies. At 31 March 1991, the Group employed 122 executive staff and 68 support and clerical staff.
7 At the time of the sale, British Technology Group:

- owned 1,708 inventions, of which 241 were under development, 637 were licensed and 830 unlicensed;
- owned 9,070 patents and patent applications to protect the 1,708 inventions; and
- had granted 485 licences representing 637 licensed inventions.

8 The management identify technologies that in their view offer the best prospect of commercial success. Selection is on the basis that the technology is capable of developing significant potential revenue over its future patentable life. Potential revenue is the income a technology is regarded as capable of generating for the Group after taking into account technical, commercial and market risks.
Appendix 2
The Committee of Public Accounts: main recommendations relevant to the sale of the British Technology Group

In reviewing the sale of the British Technology Group, the National Audit Office compared actions taken by the Department of Trade and Industry against recent recommendations made by the Committee of Public Accounts on the handling of earlier sales. A selection of the most relevant is given below.

<table>
<thead>
<tr>
<th>Issue</th>
<th>PAC Recommendation</th>
<th>Treasury Minute Response</th>
<th>Current C&amp;AG’s Report References</th>
</tr>
</thead>
<tbody>
<tr>
<td>Method of sale</td>
<td>Anything other than full and open competition should be the exception. (1st Report, 1991–92, para 7(i), HC 51)</td>
<td>The Government agrees that, wherever practical and consistent with the objectives for sale, full and open competition maximises value for money from the sale of Government assets. (1st Report HMT 1991–92, para 2, Cmd 1819)</td>
<td>Para 2.2 — The Department judged that the continuation of the company’s business could be put at risk if a single buyer was able to purchase the company outright. They therefore decided to seek bids from groups of investors rather than from single buyers and succeeded in securing indicative bids from four consortia.</td>
</tr>
<tr>
<td>Marketing</td>
<td>We ... recommend that departments continue to make a careful assessment of the most appropriate methods of sale in order to maximise proceeds. (34th Report 1987–88, para 3(iv), HC 211)</td>
<td>The Government will continue to consider, in the circumstances of each sale, the respective merits of full and tranche sales. (34th Report HMT 1987–88, paras 70–71, Cmd 559)</td>
<td>Para 2.8–2.14 — The Department considered a number of methods for privatising the company. These included a public flotation, the private placement of shares with investors, a management buyout, the sale of the company to a charitable trust and a trade sale. The Department concluded that a competitive trade sale to a consortium of investors was the best approach.</td>
</tr>
<tr>
<td>Valuation of the company</td>
<td>... we regard the reliance on &quot;discreet approaches&quot; to selected firms as unsatisfactory; and we believe that publicising the privatisation programme more widely might have secured better value for money ... (19th Report 1990–91, para 2(vi), HC 440)</td>
<td>The Government accepts the principle of open competition when privatising functions and services and that appropriate and effective publicity is a key element in attracting the maximum competition and so securing best value for money. (19th Report HMT 1990–91, para 47, Cmd 1617)</td>
<td>Para 2.23 — The Department’s financial advisers met 30 organisations and sent details and briefing material to some 200 more potential investors in the United Kingdom and overseas. In addition, a notice was published in the financial press.</td>
</tr>
<tr>
<td></td>
<td>... we expect the selling department to make their own comprehensive valuation of the undertaking to be sold ... such as by reference to a realistic estimate of the business’s future earnings or to the worth of its capital assets. (1st Report 1991–92, para 7(ii), HC 51)</td>
<td>... the Government believes that the process of determining what is, or is not, a realistic price for the assets being sold is best achieved by a competitive market ... The Government agrees that it may be appropriate, in some cases, to employ a benchmark or range of benchmarks in assessing tender bids ... The Government believes that any such benchmark will be an aid to judgement only, to be weighed against the objectives of the sale and other factors affecting the sale decision. (1st Report HMT 1991–92, para 6, Cmd 1819)</td>
<td>Para 2.15–2.19 — The Department asked their financial advisers, Price Waterhouse, to value the company, to assist them in assessing the comparative merits and the adequacy of the bids received from prospective purchasers. Price Waterhouse valued the company to be worth between £15 million and £30 million.</td>
</tr>
</tbody>
</table>
Since any under-estimates of future profit and dividend levels are likely to have the effect of depressing sales proceeds, we recommend that departments should take great care to estimate dividend and profit forecasts as accurately as possible, and, in the event that the company's Board take a different view from theirs, departments should ensure that the taxpayer's interests are protected as effectively as future shareholders' interests. (34th Report 1987–88, para 3(viii), HC 211)

We recommend that in future cases departments should ensure that they have up to date valuations, including, where appropriate, potential development values of land and other assets, before a privatisation sale. (15th Report 1989–90, para 3(v), HC 352)

In situations where a department decide not to dispose of surplus assets ahead or the main sale... we expect the department to protect the taxpayer's interest by providing for the public purse to claw back any gains arising within a reasonable period subsequent to the privatisation. Where departments consider that to include clawback provisions... might depress the price... we expect them to assess where the balance of advantage to the taxpayer may lie before they make any binding commitment either way. (1st Report 1991–92, para 7(v)–(vi), HC 51)

In any case where public assets are sold in competition, it is essential that all bidders have a complete and clear understanding of the seller's requirements. (19th Report 1991–92, para 2(v), HC 117)

The board of each privatised company is best placed to estimate the future levels of profits and dividends of the company, and has legal responsibility for any such statements included in the prospectus. However, the Government will continue to seek independent advice on the reasonableness of any estimates made by the board, and will also seek to ensure that the interests of taxpayers are taken into account to the maximum extent, while also bearing in mind the objectives of the sale and the interests of the taxpayer. (34th Report HMT 1987–88, para (vi), Cmd 509)

The Treasury endorses the importance of considering the most appropriate treatment of land and other assets. The... extent to which valuations need to be continually updated as a privatisation proceeds, will depend on a number of factors including the relative importance of the assets as such in the overall value of the undertaking. (13th Report 1989–90, para 24, Cmnd 1150)

Where separate sale is not a practical means of achieving full value in the time before sale, the surplus assets may be retained in the business to be privatised, but the Government further agrees that they should be considered as the possible subject of a clawback mechanism designed to capture a proportion of the alternative use valuation... (1st Report HMT 1991–92, para 9, Cmd 1619)

Where the relative importance of the assets as such in the overall value of the undertaking is broadly in line with the company's income. PA Consulting Group's assessment for the overall value of the undertaking was broadly in line with the company's income. PA Consulting Group's assessment was broadly in line with the company's projections.

The Government will continue to make all relevant information available to bidders in its future sales of public assets. (19th Report 1991–92, para 16, Cmd 1998)
<table>
<thead>
<tr>
<th>Issue</th>
<th>PAC Recommendation</th>
<th>Treasury Minute Response</th>
<th>Current C&amp;AG's Report References</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial</td>
<td>We are concerned that additional payments were made to advisers in circumstances</td>
<td>The Department notes the concerns of the Committee about additional payments made to</td>
<td>Paras 3.5-3.6—The Department incurred expenditure of £897,400 above their</td>
</tr>
<tr>
<td>Control</td>
<td>where there was not a clear obligation to do so and no clear evidence to support the</td>
<td>certain consultants. ... The additional payments reflect reasonable reward under the</td>
<td>September 1991 forecast for work necessarily undertaken to complete this</td>
</tr>
<tr>
<td></td>
<td>amount paid. (7th Report 1992–93, para 3(xiv), HC 140)</td>
<td>contracts for the successful completion... (7th Report 1992–93 HMT, para 104, Cmnd 2074)</td>
<td>complex sale, of which £226,300 was to advisers in excess of contracts for</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>additional work required.</td>
</tr>
</tbody>
</table>
# Appendix 3

## Timetable and key stages in the sale

<table>
<thead>
<tr>
<th>Date</th>
<th>Event</th>
<th>Management Led Consortium</th>
<th>Anglo American Consortium</th>
<th>Technology Marketing Corporation Consortium</th>
<th>Mason/Finlay Bank Consortium</th>
</tr>
</thead>
<tbody>
<tr>
<td>1988</td>
<td>April</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Government announce intention to privatise British Technology Group</td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>1991</td>
<td>Oct</td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td></td>
<td>Legislation receives Royal Assent</td>
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<tr>
<td></td>
<td>Nov</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Information Memorandum published</td>
<td>✓</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Dec</td>
<td>British Technology Group management declare their intention to form a consortium</td>
<td>✓</td>
<td></td>
<td></td>
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<tr>
<td>1992</td>
<td>6 Jan</td>
<td>Indicative bids</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>12 Jan</td>
<td>Draft Sale and Purchase agreement sent to consortia</td>
<td>✓</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>20–24 Jan</td>
<td>Data Rooms made available</td>
<td>✓</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>18 Feb</td>
<td>Mason/Finlay Bank consortium withdraw from bidding</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>19 Feb</td>
<td>Formal bids</td>
<td>✓</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>21 Feb</td>
<td>Technology Marketing consortium bid declined</td>
<td>✓</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>21 Feb</td>
<td>Volume 3 of the Long Form Report made available to the two remaining consortia</td>
<td>✓</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>27 Feb</td>
<td>Final bids</td>
<td>✓</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>4 Mar</td>
<td>Dept decide to enter into exclusive negotiations with management-led consortium</td>
<td>✓</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>6 Mar</td>
<td>Sale details agreed</td>
<td>✓</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>10 Mar</td>
<td>Sale and Purchase Agreement signed</td>
<td>✓</td>
<td></td>
<td></td>
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<tr>
<td></td>
<td>31 Mar</td>
<td>Completion</td>
<td>✓</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1993</td>
<td>30 Mar</td>
<td>Nil settlement agreed for completion accounts</td>
<td>✓</td>
<td></td>
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</tr>
</tbody>
</table>
Appendix 4
Information about the business

A Information provided in the data rooms

Financial performance
- Audited accounts for the three years to 31 March 1991. Most recent accounts for subsidiary and associated companies, and investments held for resale
- Tax computations for the previous six years

Financial projections
- Corporate and business plans showing the company’s own projections of aggregate gross and net income over ten years
- Breakdown of capital expenditure to which the company was committed and how these projections were to be funded

Accountants’ report
- The reporting accountants’ Long Form Report (Volumes 1&2) which documented aspects of the business including its organisation, staffing, management systems, the financial performance of the company and an evaluation of the company’s ten year aggregated projections

Assets
- Freehold title deeds, leasehold agreements and title reports
- Valuation reports on the company’s freehold property
- Description of the main technologies with summary financial information showing projections of gross and net revenue for each technology
- Specimen standard licences that companies wanting to use technologies were required to sign
- Specimen standard revenue sharing agreements that describe the standard terms agreed with inventive sources for sharing revenues
- Lists of all licences, revenue sharing agreements, patents and patent applications

No specific financial information was supplied on individual licences and agreements

BTG Pension Fund
- Valuation of the pension fund at 1 April 1990
- The pension fund trust deed
- Staff booklet on the pension scheme
- The trustees’ latest annual report on the pension fund

Management and staff
- Specimen standard service contract documenting the terms of employment
- Directors’ service contracts and the provisions of the employee profit sharing scheme
B Additional information promised to bidders

In January 1992 Price Waterhouse informed the bidders that all licences, revenue sharing agreements, patents and patent applications would be available at the company's offices for inspection on request.

C Information requested by the four consortia

After visiting the data room, the leaders of the four consortia requested additional information from Price Waterhouse, as follows:

(i) Anglo-American Consortium
- Key licence agreements and projections of future revenues, and access to details of royalties for a minimum of 32 specified technologies
- The related revenue sharing agreements
- Access to the reporting accountants' Long Form Report (Volume 3) which gave details of revenue projections for key technologies
- Projected investment and capital commitments
- Full breakdown of the 1992 balance sheet
- Access to senior management
- Access to the authors of the Long Form Report
- Tax breakdowns
- Costs breakdown
- Computer systems costs
- Discretionary and committed investment expenditure
- Working capital requirements
- Details of vesting arrangements
- Analysis of pension contributions
- Non-standard service contracts
- Property revaluation resources

(ii) Management-Led Consortium
- Monthly cash flow forecast projections (minimum 12 months)

(iii) Mason/Finlay Bank Consortium
- Detailed cash flow projections to enable the performance of sensitivity analyses

(iv) Technology Marketing Corporation Consortium
- How irreversible are capital commitments?
- Why have capital commitments dropped £4 million between March and December 1991?
- Age, salary and length of service details of all employees

In response, Price Waterhouse provided:
- Details from some licence agreements
- Access to the company's senior management
- An analysis of net current assets at 31 December 1991
- Access to the reporting accountants to discuss the Long Form Report
Prior to final competitive bids the Department made available the following information to the two competing consortia:

- Volume 3 of the reporting accountants' Long Form Report which gave details of revenue projections for key technologies
- A cash flow statement for the year to 31 December 1991.
Appendix 5
Advisers appointed by the Department of Trade and Industry

i) Principal advisers
Price Waterhouse — Financial advisers
Clifford Chance — Legal advisers
Coopers and Lybrand — Reporting accountants

ii) Other advisers
PA Consulting Group — Technical advisers
Debenham, Tewson and Chinnocks — Property valuers
Government Actuary’s Department — Actuarial advisers