

**EXPLANATORY MEMORANDUM TO
THE TAKEOVERS DIRECTIVE (INTERIM IMPLEMENTATION REGULATIONS)
2006**

2006 No. 1183

1. 1.1 This explanatory memorandum has been prepared by the Department of Trade and Industry and is laid before Parliament by Command of Her Majesty.
- 1.2 This memorandum contains information for the House of Lords Select Committee on the Merits of Statutory Instruments and the Joint Committee on Statutory Instruments.

2. Description

The instrument implements Directive 2004/25/EC of the European Parliament and of the Council on Takeover Bids (“the Takeovers Directive”) by:-

- placing takeover regulatory activities of the Panel on Takeovers and Mergers¹ (“the Takeover Panel”) within a wholly statutory framework for the first time;
- adopting substantive rules which apply to the conduct of takeover bids covered by the Takeovers Directive;
- making provision concerning the override of “barriers to takeovers” in certain circumstances;
- imposing additional disclosure requirements on certain companies; and
- laying down provisions addressing the problems of, and for, minority shareholders following a successful takeover bid.

3. Matters of special interest to the Joint Committee on Statutory Instruments

3.1 **Interim application of the instrument.** Substantive measures related to takeover regulation are currently contained in the Company Law Reform Bill (Part 22) which was introduced in the House of Lords on 1 November 2005. The intention is that the instrument will be revoked in its entirety as soon as the takeovers provisions of the Bill become law.

3.2 **Takeover Panel.** The instrument will extend new statutory powers to the Takeover Panel in respect of certain of its takeover regulatory functions. For instance, the Panel will be able to require information and documents, apply to the court for enforcement of its decisions and impose sanctions on those who transgress the takeover rules.

3.3 **Adoption of the Takeover Code.** In the UK, rules related to takeover regulation have historically been contained in “The City Code on Takeovers and Mergers” (“the Takeover Code”). This body of rules has been previously laid down by

¹ Further information about the Takeover Panel is available on the Panel’s website at <http://www.thetakeoverpanel.org.uk/new/>.

the Takeover Panel, essentially on a non-statutory basis. The Takeover Code has been amended by the Takeover Panel to bring it into conformity with obligations in the Takeovers Directive. The instrument gives effect to that part of the revised Code that implements the Directive.

4. Legislative Background

EU Takeovers Directive

4.1 The instrument implements, on an interim basis, the Takeovers Directive². The Directive lays down minimum rules concerning the regulation of takeovers of companies governed by the laws of EU Member States³ and whose shares are traded on a regulated market⁴. The Takeovers Directive was adopted on 21 April 2004 and must be implemented by Member States no later than 20 May 2006. A copy of the transposition notes, which explain how the instrument transposes the Takeovers Directive, is being sent separately to the House of Lords Select Committee on the Merits of Statutory Instruments and the Joint Committee on Statutory Instruments.

4.2 The Takeovers Directive contains:-

- A regulatory framework for bodies that supervise takeover bids;
- General principles that apply to the conduct of takeover bids;
- Basic rules about takeover bids (for instance, about when a takeover bid must be made and the price that must be paid to shareholders, the contents of offer documents prepared by a takeover bidder, requirements to inform employees and the time period a takeover bid will be open for);
- Provisions restricting barriers to takeovers (such as action that might be taken to prevent a takeover by a company or its board of directors);
- Disclosure requirements for companies; and
- Provisions dealing with the problems of, and for, residual minority shareholders following a successful takeover bid (known as “squeeze-out” and “sell-out”).

4.3 The Takeovers Directive was considered legally and politically important and was subject to extensive scrutiny in both Houses of Parliament. In particular, the House of Lords Select Committee on the European Union undertook two enquiries into the Directive, reporting in the 1995-96 and 2002-03 sessions⁵. The Directive was also subject to debate in the House of Commons European Standing Committee C⁶. Key issues considered by both scrutiny Committees included the extent to which the minimum standards approach adopted by the Directive really would increase the effectiveness of takeover regulation across the EU and the degree to which the Directive should address in substance barriers to takeovers. Equally importantly, the Committees examined whether the placing of the domestic takeover regulatory regime within a statutory framework, as the Directive requires, would lead to an increase in “tactical litigation” (litigation to frustrate and delay takeover bids).

² European Directive on Takeover Bids (2004/25/EC)

³ “Member States” includes the three States that make up the EEA

⁴ Regulated markets are defined by article 1(13) of Directive 93/22/EEC. A financial market (e.g. a Stock Exchange) may ask to be designated as a “regulated market” if it meets conditions laid down. A list of regulated markets in the United Kingdom is situated on the website of the Financial Services Authority at http://www.fsa.gov.uk/register-res/html/prof_exchanges_fram.html

⁵ “Takeover Bids” (13th Report, 1995-96, HL Paper 100) and “If At First You Don’t Succeed... Takeover Bids Again” (28th Report, 2002-03, HL Paper 128).

⁶ “Takeover Bids”, European Standing Committee C, Session 2002-03, 19 March 2003

Takeover Regulation in the UK

4.4 Historically, very few provisions related to takeover regulation have been contained in statute (the only substantive legislative provisions are at Part 13A of the Companies Act 1985 (Part 14A of the Companies (Northern Ireland) Order 1986), and relate to squeeze-out and sell out rights.

4.5 The Takeover Panel is the regulatory body which administers the Takeover Code (both making the rules in the Takeover Code and enforcing them). Its central objective is to ensure equality of treatment and opportunity for all shareholders in takeover bids. The Takeover Panel was set up in 1968. The concept was proposed by the Governor of the Bank of England and the Chairman of the Stock Exchange in response to mounting concern about practices unfair to shareholders which had featured in a number of controversial takeovers. Between 1968 and 2005 the Takeover Panel handled some 7,000 announced offers and, in addition, approximately half as many cases where no offer was, in the event, announced.

Company Law Reform Bill

4.6 Substantive provisions to implement the Takeovers Directive are contained at Part 22 of the Company Law Reform Bill. The Bill will not, however, have completed Parliamentary passage by 20 May 2006, by when the Takeovers Directive must be implemented. The instrument substantially follows the approach in the Company Law Reform Bill, with the following four important differences:-

a.) Types of transactions - The instrument will only apply to takeover bids covered by the Takeovers Directive. The Bill provisions will apply more widely to other types of transactions which may have an effect on the ownership or control of companies, such as takeovers of public companies whose shares are not traded on a regulated market and mergers.

b.) Panel's Rule-making Power - In regulations made under section 2(2) of the European Communities Act 1972, it is not possible to give the Panel power to make and amend rules which have statutory effect. The Panel will not, therefore, during the period between 20 May 2006 and the entry into force of the relevant provisions of the Bill, be able to adopt amendments to the Takeover Code in so far as they relate to matters contained in the Takeovers Directive. Instead, the instrument gives effect to the Code as it stands immediately before the instrument was made (i.e. the Code as amended to ensure conformity with the Takeovers Directive). The Bill includes a rule-making power which, once it becomes law, will enable the Panel to make and amend rules both in relation to transactions covered by the Takeovers Directive and other types of transactions which may have an effect on the ownership or control of companies.

c.) Squeeze-out and sell-out provisions - The instrument substantially replicates those squeeze-out and sell-out provisions already contained in the Companies Act 1985 and the Companies (Northern Ireland) Order 1986, with changes either necessary to implement the Takeovers Directive or arising out of or related to obligations in the Directive. Further unrelated changes being made by the Bill to reflect recommendations made by the Company Law Review (an independent review of

company law sponsored by the Department of Trade and Industry which reported finally in 2000) will not be included.

d.) Offences - Certain offence provisions under the Regulations (for instance, in relation to unlawful disclosure of information subject to secrecy provisions) will apply in a different way to those under the Bill. They will be restricted to matters covered by the Takeovers Directive. Similarly, the maximum penalties that may be imposed under the Regulations are restricted by the powers in the European Communities Act 1972.

Parliamentary Counsel

4.7 As the instrument amends primary legislation and is substantially based on the provisions at Part 22 of the Company Law Reform Bill concerning takeovers, it has been considered in draft by Parliamentary Counsel.

5. Extent

This instrument applies to all of the United Kingdom.

6. European Convention on Human Rights

Mr Gerry Sutcliffe, Parliamentary Under Secretary of State for Employment Relations and Consumer Affairs, has made the following statement regarding Human Rights:

“In my view the provisions of the Takeovers Directive (Interim Implementation) Regulations 2006 are compatible with the Convention rights.”

7. Policy background

EU Takeovers Directive – Negotiations

7.1 Political agreement to a Directive on takeover bids was an objective of the Financial Services Action Plan⁷, agreed by Heads of State and Government at the Lisbon Summit in 2000 for completion by 2005 and with the aim of creating an integrated financial market within the EU. Despite the political consensus on the desirability of a Directive in this area, negotiations on the Directive had a long and difficult history from the publication of the first Commission proposal in 1989. The critical issue in the later stages of negotiations was the extent to which the Directive should, in substance, override the barriers to takeovers which existed in a number of EU Member States.

EU Takeovers Directive – Implementation

7.2 A full public consultation exercise on implementation of the Takeovers Directive was undertaken from January 2005⁸ onwards. The Government response to this consultation exercise, together with draft clauses to implement the Directive

⁷ “Financial Services: Implementing the Framework for Financial Markets: Action Plan”, communication of the EU Commission (COM (1999) 232, 11.05.99) available on the Europa website: http://europa.eu.int/comm/internal_market/finances/docs/actionplan/index/action_en.pdf.

⁸ “DTI – Company Law – Implementation of the European Directive on Takeover Bids – A Consultative Document” (January 2005, DTI/Pub 7710/0.8k/01/05/NP URN 05/511 (available on the DTI website: <http://www.dti.gov.uk/cld/currentdocs.htm>).

through the Company Law Reform Bill were published on 17 July 2005⁹. Further details concerning the outcome of the consultation are contained in the Regulatory Impact Assessment which accompanies this memorandum. Guidance on the interim regime to be given effect to by the current instrument together with a draft of the instrument were placed on the website of the Department of Trade and Industry in March 2006¹⁰.

Takeover Panel Rules

7.3 In November 2005, the Takeover Panel published a full public consultation document¹¹ on the changes necessary to make the rules in the Takeover Code wholly consistent with the requirements of the Takeovers Directive. Those changes, amended in the light of consultation, were adopted by the Code Committee of the Panel on 11 April 2006. A full response statement to the consultation exercise, setting out all the changes, was published by the Panel on 21 April 2006. The Takeover Code adopted by this instrument includes those changes. The Code and all the amendments made are available on the Takeover Panel's website. A new edition of the Code, incorporating all the changes, will be published shortly before 20 May 2006.

8. Impact

8.1 A Regulatory Impact Assessment is attached to this memorandum.

8.2 The impact on the public sector is expected to be minimal. Regulation of takeover bids will remain a matter for the Takeover Panel, which will continue to be independent of Government.

9. Contact

Mike Edbury at the Department of Trade and Industry (telephone number: 0207 215 0231 or e-mail: Michael.Edbury@dti.gsi.gov.uk) can answer any queries regarding the instrument.

⁹ "DTI – Company Law – Implementation of the European Directive on Takeover Bids - Government Response and Summary of Responses to the Consultative Document" together with draft clauses available on the DTI website <http://www.dti.gov.uk/cld/clauses.htm>

¹⁰ "Implementation of the EU Directive on Takeover Bids - Guidance on changes to the rules on company takeovers" available on DTI website: <http://www.dti.gov.uk/cld/hottopics.htm>.

¹¹ A copy of the consultation paper, "The Implementation of the Takeovers Directive – Proposals relating to amendments to the Takeovers Code", is available on the Panel's website <http://www.thetakeoverpanel.org.uk/new/>. The consultation closed on 10 February 2006.

Regulatory Impact Assessment

The Takeovers Directive (Interim Implementation) Regulations 2006

Implementation of Directive 2004/25/EC of the European Parliament and of the Council of 21 April 2004 on Takeover Bids (“the Directive”)

Purpose and Intended Effect of Measure

Objective

1. The Directive lays down minimum standards in relation to the regulation of takeovers of companies and provides for the protection of their shareholders. It will apply, with effect from 20 May 2006, to the regulation of takeover bids for companies incorporated in the EU (and EEA¹²) whose shares are admitted to trading on a regulated market in the EU.

2. Provisions substantively implementing the Directive are contained in Part 22 of the Company Law Reform Bill which is currently before Parliament. However, the Bill will not have completed Parliamentary passage before 20 May 2006. The Takeovers Directive (Interim Implementation) Regulations 2006 (“the Interim Regulations”) are, therefore, intended to implement the Directive on an interim basis until the relevant provisions in the Company Law Reform Bill come into force.

Summary of the Directive provisions and the current position under UK law

3. The Directive is a “minimum standards” Directive. It lays down a basic level of rules that Member States are required to make in relation to takeover regulation. It is open to Member States to make more detailed provisions than are required by the Directive. In general terms, the existing system of takeover regulation in the UK, overseen by the Panel on Takeovers and Mergers (“the Panel”) already recognises most of the rules required by the Directive and involves further more detailed regulatory rules and procedure. This will continue to be the case after the Directive has been implemented.

4. The Directive applies to the United Kingdom, as do the Interim Regulations.

5. The main features of the Directive are as follows:-

- A.) *A regulatory framework for bodies that supervise takeover bids*

¹² All further references in this Regulatory Impact Assessment to “EU” also include the three States that make up the EEA.

Presently, the supervision of takeover bids in the United Kingdom is undertaken by the Panel, essentially on a non-statutory basis. It is intended that the Panel's takeover regulatory responsibilities will continue after implementation of the Directive. However, regulatory activities of the Panel following implementation of the Interim Regulations will be in the context of a statutory framework.

- *B.) General principles that apply to the conduct of takeover bids*

General principles are laid down in the City Code on Takeovers and Mergers ("the Code"), which is the body of rules for which the Panel is responsible. These general principles are now the same as those contained in the Directive.

- *C.) Basic rules about takeover bids (for instance, about when a takeover bid must be made and the price that must be paid to shareholders, the contents of offer documents prepared by a takeover bidder, requirements to inform employees and the time period a takeover bid will be open for)*

Rules relating to these matters are contained in the Code. These rules are wholly consistent with the Directive.

- *D.) Provisions restricting barriers to takeovers (including action that might be taken to prevent a takeover by a company or its board of directors following the launch of a bid as well as defensive mechanisms that may be put in place prior to a bid being launched (such as special voting rights or limits on share ownership contained in the articles of association of a company))*

The Code contains provisions restricting action that may be taken by the management of a target company to frustrate a takeover bid without the approval of shareholders at the time of the bid. These are consistent with the Directive requirements.

There are, however, presently no provisions in UK law relating to override of defensive devices that may be put in place prior to a bid being launched. There is a Member State option to make these provisions voluntary (companies need only adopt such provisions if they choose to do so).

- *E.) Disclosure requirements for companies whose shares are traded on a regulated market (in relation to control and governance matters, etc.)*

Generally, this information is already required to be disclosed under UK law. However, the Directive requires that this information be contained in the annual report of the company and that explanatory material be provided to the annual general meeting. These requirements are new.

- *F.) Provisions dealing with the problems of, and for, residual minority shareholders following a successful takeover bid (known as “squeeze-out” and “sell-out”).*

These provisions enable a successful bidder to compulsorily purchase the shares of remaining minority shareholders and for those shareholders to require the majority shareholder to purchase their shares. They are broadly consistent with existing provisions in UK companies' legislation, although some modifications are being made to those provisions to make them wholly consistent with the Directive provisions.

Background

6. A Directive on takeover bids has been under consideration since 1985. A first proposal made by the Commission in 1989 included detailed rules on which it became clear it would be difficult to obtain agreement in Council.

Consequently, a revised proposal was published by the Commission in 1996 on the basis of a framework Directive containing general principles but leaving considerable latitude for Member States and the relevant takeover supervisory authorities to deal with the detailed implementation of those principles.

7. After discussions within the European Parliament and the Council, a joint text of a Directive on takeover bids was approved by the Conciliation Committee on 6 June 2001 but failed on a tied vote to be adopted by the European Parliament on 4 July 2001.

8. Following the narrow failure of a Directive on takeover bids to be adopted in 2001, the Commission appointed a High Level Group of Company Law Experts to examine a number of issues related to takeovers which the Commission considered to have been of concern to the European Parliament, principally the issue of ensuring a “level playing field” for shareholders (or the existence of different share and control structures) across the EU. The High Level Group reported on those issues in January 2002 and the Commission presented a new proposal for a Directive in October 2002. Following further detailed discussions, the present Directive was finally adopted on 21 April 2004.

9. At present, the Panel and the Code rules which it administers seek to secure the fair treatment of all shareholders and create an orderly framework for the conduct of takeover bids. In particular, the Panel will police any conflict between the parties where the bid is a hostile one (i.e. not recommended for acceptance by the board of the offeree).

10. Since the Panel was established in 1968, it has overseen over 7,000 announced takeover offers and, in addition, approximately half as many cases where no offer was, in the event, announced. In the year ending 31 March 2005, there were 114 finalised “takeover” transactions, of which 99 involved a change of control (the corresponding figures for the year to 31 March 2004 (were 136 and 110, respectively).

11. The key strengths of the present system of takeover regulation overseen by the Panel can be summarised as follows:

- flexibility, speed and certainty in decision-making;
- independence and regulatory autonomy;
- principles-based regulation;
- involvement of key City and business participants in developing takeover rules and the regulatory framework;
- professional expertise in regulatory activities, notably through Panel membership and secondments; and
- consensual approach to regulation amongst market participants.

12. The Government wishes to preserve, as far as possible, these core characteristics of takeover regulation.

Risk Assessment

13. Implementation of the Directive through the Interim Regulations does open up the prospect of improved shareholder protection and access to capital markets across Europe. It can act as a stimulus for more transparent corporate governance structures with extended shareholder involvement. It could also encourage cross-border takeover activity and, potentially, consequential improvements in corporate management and performance, benefiting all those with a stake in the markets. Additionally, the negotiations on the Directive, and subsequent discussions between Member States and regulators on implementation issues, have contributed to “soft harmonization” (that is, convergence of takeover regulatory regimes as a side consequence of the legislative process).

14. Nevertheless, the Directive leaves Member States considerable scope in implementing to adopt different approaches and rules. In particular, the key articles of the Directive which address barriers to takeovers across the EU have been made optional (Member States need not impose these on their companies). The statutory reinforcement by the Directive of different approaches on key issues of corporate regulation may lead to a divergence of practice, rather than increased unity in approach. It is not possible through the Interim Regulations to influence decisions taken by other Member States as to the appropriate

implementing provisions and so to seek to reduce the scope for different approaches to be taken.

15. Should Member States not impose (or companies, influenced by markets, not choose to adopt) more open capital and governance structures as a consequence of the Directive, possible benefits in terms of improving the efficiency of firms in the EU as a consequence of the increased likelihood of takeovers will diminish. This could lead to higher costs associated with the survival of inefficient businesses. This will be the case if efficient EU or non-EU companies are unable to takeover inefficient EU ones and if inefficient EU companies are allowed to takeover efficient ones. Similarly, the presence of inefficient companies may also inhibit competition which could be improved via lower barriers to competition, that is by making the threat of takeover more credible.

16. It is also the case that the Directive does not address barriers to takeovers falling outside legal or regulatory structures (such as different cultural approaches to corporate restructuring amongst Member States and differing patterns in ownership and control (such as dominant single shareholders in companies)). Again, it is not possible in the context of the domestic implementing legislation to minimise the extent of such barriers to takeover activity within the EU as a whole.

17. Such factors, which might impair competition in EU markets, could also affect the competitiveness of EU companies in the global marketplace. Ultimately, the risk that inefficient EU companies might survive and prevail could lead to higher prices for consumers and welfare losses as a result of resources being inefficiently used by these companies.

18. Additionally, the Interim Regulations will not significantly increase protections for shareholders of companies registered and traded on financial markets in the UK, nor improve the effectiveness of the Panel or the Code. However, they might give rise to an increased risk of litigation within the bid process, which could have the effect of delaying or frustrating a takeover bid and hindering the opportunity for shareholders to consider the benefits of the bid. This would undermine the openness and fluidity of the domestic takeover market (see further paragraphs 44 to 47).

19. Finally, the fact that the Directive applies solely to companies traded on a regulated market may lead to certain companies seeking to avoid the consequences of the effects of the Directive by transferring to alternative markets (whether within or outside the EU). This again could lead to greater diversity of approach, both in relation to takeover activity and other types of corporate activity, which would mitigate against greater competition and more transparent markets. This also falls beyond the scope of Interim Regulations implementing the Directive domestically.

20. There is, clearly, a tension between the features of the Directive which lead to a common approach towards takeover regulation and, thus, enhance EU Single Market objectives and the minimum standards and optional provisions within the Directive which might encourage diversity of approach. This must be viewed in the wider context of global markets and the original aims of the Directive, as part of the Lisbon Agenda to foster the competitiveness of the EU Single Market in financial services. In particular, it is difficult to assess the consequences of the implementation of the Directive on cross border restructuring activities involving companies registered in countries outside the EU. This will depend on whether the EU is perceived as having a more integrated takeover market.

The Options for Implementation

Option 1 – Do Nothing

21. Option 1 is a non-starter. Not implementing the Directive could lead to the Government facing infraction proceedings before the European Court of Justice since, under Community law, the provisions of the Directive have to be implemented by rules which have legally binding effect in some way. Currently, whilst there are substantive rules under the Code, there are no statutory provisions in the UK in many of the areas of takeover regulation covered by the Directive.

Option 2 – Direct Statutory Provision

22. It would be possible to make provision (which could be done by regulations made under section 2(2) of the European Communities Act 1972) comprehensively setting out the rules necessary to implement the Directive (or adopting a version of the Code which was consistent with the Directive). The provisions would need to designate a supervisory body such as the Panel and provide it with the necessary powers. However, this approach leads to two problems, as follows:

- it would not be permissible under section 2(2) to delegate a rule-making power to the Panel to amend the Code; and
- although section 2(2) is wide enough to enable provision for matters arising out of, or related to, implementation of the Directive, all that might be necessary to produce a single regime, rather than parallel ones, could only be achieved through primary legislation. At present, the Panel regulates a number of matters which are not covered by the Directive. An example of this is takeover bids for public companies which are not admitted to trading on a regulated market. This would create two parallel systems of takeover regulation, one of which fell within the statutory scope of section 2(2) regulations and one of which did not.

Option 3 – Give Recognition to the Takeover Code

23. A radically different approach would be to provide that failure to comply with the requirements of the Code as applied by the Panel became a breach of, for example, the Listing Rules made under Part 6 of the Financial Services and Markets Act 2000 (“the Listing Rules”). The Panel would continue to make and apply rules under the Code as at present. This would build upon the fact that both the jurisdiction and authority of the Panel and the Code are already expressly or implicitly recognised by the legislation and the courts. Such an approach would certainly require secondary legislation under section 2(2) of the European Communities Act, and may require primary legislation, but could avoid the need to include detailed rules or to confer an express rule-making power related to takeovers within the framework of that legislation.

24. However, other important issues related to the constitution and powers of the Panel would still remain to be dealt with and such an approach to implementation has a number of further drawbacks:

- there are considerable legal uncertainties, in particular, as to whether recognition of a non-statutory Code as applied by a non-statutory body (even with the back-up of the Listing Rules or other statutory support) would constitute proper implementation of the Directive;
- such an approach would not remove the need to deal with a number of other issues relating to, for example, constitution, funding, control and liability of the Panel;
- an approach to sanctions focusing on infringement of the Listing Rules would not effectively regulate certain key parties to takeover bids, including, for example, financial advisers, lawyers and shareholders.

Option 4 – Delegated Statutory Powers

25. The Directive could be implemented through replicating, to the greatest extent possible, the Panel’s current jurisdiction, practices and procedures within a statutory framework, including giving the Panel the power to make statutory rules. Primary legislation would definitely be needed to avoid breaching the principle against sub-delegation.

26. The Government has concluded that, in order to maintain the advantages of the current regime, the most transparent, effective and legally certain means of proceeding would be to place the regulatory activities of the Panel within a legislative regime in primary legislation. Provisions to this effect are contained in the Company Law Reform Bill currently being considered by Parliament. However, that Bill will not have completed Parliamentary passage prior to 20 May 2006, by which date the Directive must be implemented. Consequently, there is no available primary legislative vehicle by which implementation may be achieved within the due date.

Summary of options

27. Only options 2 and 3 are further considered. Option 1 would not give legal effect to the Directive. Option 4 is not possible due to timetable constraints. A summary of the key benefits, costs and risks associated with options 2 and 3 is set out at Annex A. These are described in more detail in the body of this Assessment.

Interim Nature of the Regulations

28. Before turning substantively to the benefits and costs of the implementing options, it is important to stress the short term nature of the proposed Interim Regulations. The provisions substantively implementing the Directive are contained in the Company Law Reform Bill which is currently being considered by Parliament. It is intended that the Interim Regulations will be repealed and replaced by the provisions currently contained in the Bill. It is not possible to estimate the precise date at which the Bill will complete Parliamentary passage and receive Royal Assent, but for the purpose of this Impact Assessment, it is assumed that the Interim Regulations will be repealed in December 2006, i.e. 7 months from their coming into force. The costs and benefits of the Interim Regulations only, therefore, apply during a restricted period of time.

Benefits and Costs – Sectors and Groups Affected

29. The Directive applies to companies whose shares are admitted to trading on a regulated market and registered in a Member State. There are approximately 1,700 companies which are both incorporated and traded in the UK and around a further 500 companies incorporated outside the UK but traded in the UK (such companies will only fall within the scope of the implementing regulations where they are also registered in an EU Member State). Such companies will fall within all sectors of business and the Directive is not, therefore, restricted to particular sectors or groups.

30. The Directive does not apply to private limited companies or to public limited companies which are not admitted to trading on a regulated market. For the purposes of ensuring a consistent regulatory takeover regime for all companies and transactions, there would be benefits in providing that the Code administered by the Panel (but now within a statutory framework) will continue to apply to certain companies not covered by the Directive as it does presently. However, it is not possible under the powers contained in the European Communities Act 1972 to make provision for takeover transactions not falling within the scope of the Directive. Accordingly, under neither option 2 or 3 is it possible to facilitate the continuation of the present situation where one rule-book, the Code, applies to all “takeover transactions” during the period for

which the Interim Regulations apply irrespective of whether or not they would fall within the scope of the Directive.

Benefits – Economic

31. The principal benefits likely to arise from implementation of the Directive are in relation to the possible encouragement of cross-border takeover activity as a central element of the EU Financial Services Action Plan¹³. Takeover activity can serve to exploit business synergies, act as a discipline upon corporate management and allow shareholders to sell their shares for a price above the existing market value. Such advantages can benefit all those with a stake in the markets, whether directly or indirectly (such as through pensions funds). There are a number of specific provisions in the Directive that should be helpful in freeing up the market and making it more transparent following implementation. These measures are set out below. These benefits are not affected irrespective of whether implementing option 2 or 3 is chosen. It is, however, stressed that in the domestic implementing legislation it is not possible to affect implementing decisions taken by other Member States on which the wider economic benefits of the Directive, as opposed to the domestic implementing legislation, are heavily dependent.

Mandatory Bid Requirement

32. Article 5 of the Directive requires Member States to introduce a rule, where a party acquires a controlling interest in a company, that a bid be made for all the remaining shares (the so-called mandatory bid requirement). Article 5 reflects one of the key requirements in the Code. Without a mandatory bid requirement, shareholders will have no right of exit from the company which they may consider essential since their rights may, in effect, become subservient to those of a single dominant controlling shareholder. Moreover, they would not be able to benefit from the “control premium” attributable where the real control of a company changes hands. However, the Directive does not specify the threshold at which a mandatory bid has to be tabled (which in the Code is set at 30% of voting rights). This is left to individual Member States to determine. Accordingly, Member States could set a very high threshold and thereby limit the protection offered to shareholders. In adopting the existing mandatory bid threshold in the UK, the Interim Regulations seek to strike a balance between ensuring an appropriate level of minority shareholder protection whilst not unduly restricting takeover bid activity. **The Interim Regulations will, therefore, achieve no benefits as regards domestic takeover regulation as they simply reflect the existing position.**

Equitable Price

¹³ “Financial Services: Implementing the Framework for Financial Markets: Action Plan”, communication of the EU Commission (COM (1999) 232, 11.05.99) available on the Europa website: http://europa.eu.int/comm/internal_market/finances/docs/actionplan/index/action_en.pdf.

33. Article 5 of the Directive sets out the provision on “equitable price”. Laying down an EU rule on equitable price has the advantages of providing greater certainty across the EU as to the bid price to be paid in different Member States and achieving equivalent levels of shareholder protection. The equitable price is, broadly, the highest price paid by the offeror for the same shares during the period of not less than six months and not more than twelve months before the bid is tabled. Member States have the option to set the period within those parameters. When making a takeover bid, the offeror has to offer the offeree’s shareholders a price equivalent to at least the equitable price. In addition if, after the bid has been made public and before the offer closes for acceptances, the offeror purchases shares at higher than the offer price, the offeror has to increase the price so that it is not less than the highest price for the shares so acquired. Moreover, if the offeror’s offer does not consist of shares admitted to trading on a regulated market (i.e. they are shares which are not listed and therefore cannot easily be traded) or the offeror has purchased for cash securities carrying more than 5% of the voting rights in the offeror company during the relevant time period the offeror has to offer a cash alternative. The Code requires a mandatory bid to be in cash or to include a cash alternative in all cases. **The Interim Regulations will, therefore, achieve no benefits as regards domestic takeover regulation as they simply reflect the existing position.**

Disclosure by Companies of Control and Structure of their Shares

34. Articles 10(1) and 10(2) of the Directive require companies to provide, in their annual reports, detailed information on their share and control structures. This includes the following: structure of the share capital; restrictions on transfer of securities; significant shareholdings; shareholders with special control rights and a description of those rights; system of control of any employee share schemes; restrictions on voting rights; agreements between shareholders which may restrict transfers of securities or voting rights; rules governing the appointment and replacement of board members and changes to the articles; powers of board members to issue or buy back shares; significant agreements to which the company is a party which take effect, alter or terminate upon a change of control of the company following a takeover bid; and agreements providing for compensation to board members or employees resulting from resignation or redundancy following a takeover bid.

35. Article 10(3) requires the boards of companies to present an explanatory report to shareholders on the above issues at the company’s annual general meeting.

36. The disclosure requirements in articles 10(1) and 10(2) are broadly consistent with existing disclosure requirements under UK law and regulatory provisions (for instance, details relating to the structure of share capital and restrictions on transfer of shares will be contained in a company’s articles). However, the requirements to provide the information in a consolidated format

is new, as is the requirement in article 10(3) to report annually to shareholders. The latter requirement will be met by including some additional narrative text in the directors' report alongside the information required by articles 10(1) and 10(2).

37. The intention behind the requirements of article 10 is to help break down barriers to takeovers and to bring greater transparency to the market. By requiring companies to disclose share structures and so forth which clearly disadvantage certain shareholders and act as a disincentive to new investment (such as share structures which give disproportionate voting rights to certain shareholders) companies may be encouraged to change to more open systems such as share structures which consist solely of one share, one vote. The requirements apply to all companies whose shares are admitted to trading on a regulated market whether or not they are involved in a takeover. Accordingly, the requirements will apply to all EU registered companies which have shares traded on a regulated market. **As these requirements are included for the first time in the Interim Regulations, the benefits arising will apply to UK companies and their shareholders.**

Frustrating Action

38. Article 9 of the Directive restricts the management of an offeree company from taking action to frustrate a bid (i.e. with the intention of delaying or stopping a bid) without the prior authorisation of shareholders at a general meeting given for this purpose during the period of acceptance of the bid. Article 9 cites, specifically, the issuing of new shares as an example of frustrating action. Article 9 is closely in line with key provisions of the Code which are central to minority shareholder protection.

39. However, under the Directive, Member States may decide not to impose article 9 on all relevant companies. In this case, they must allow, under their national implementing legislation, companies to opt back in on a voluntary basis, and therefore be subject to the requirements of article 9, if they receive the agreement of their shareholders at a general meeting. It is the intention of the UK to implement article 9 which will, therefore, continue the protection from which UK shareholders already benefit under the Code. **The Interim Regulations will, therefore, achieve no benefits as regards domestic takeover regulation as they simply reflect the existing position.** Market pressure may also dictate that EU companies, which are not subject to article 9 through their Member States' implementing legislation, will nevertheless adopt more transparent and liberal regimes.

Squeeze-out and Sell-out

40. The concepts of "squeeze-out" and "sell-out" are designed to address the problems of, and for, minority shareholders following a successful takeover bid. Squeeze-out rights enable a successful bidder to compulsorily purchase the

shares of remaining minority shareholders who have not assented to the bid. Sell-out rights enable minority shareholders, in the wake of such a bid, to require the majority shareholder to purchase their shares. As such rights involve the compulsory purchase or acquisition of shares against the will of the holder of the shares or the acquirer, high thresholds apply to the exercising of such rights and there are protective rules on the price that must be paid for the shares concerned.

41. Such rights, both facilitating corporate restructuring and improving shareholder protection, have long been a feature of UK companies' legislation. Adjustments to the UK provisions will need to be made to these existing provisions to bring them wholly in line with the Directive, for instance in respect of calculation of the relevant thresholds and time periods which determine the exercise of such rights. However, it is not considered that these changes will change in substance the present operation of these provisions.

42. Additionally, UK shareholders in companies registered in other EU states will receive the same or similar protection to shareholders in UK companies. **The Interim Regulations will, therefore, achieve no benefits as regards domestic takeover regulation as they simply reflect the existing position.**

Benefits – Environmental and Social

43. Implementation of the Directive would appear not to include any environmental or social benefits.

Costs – Economic

Litigation

44. The costs of implementation of the Directive are largely the same, irrespective of whether option 2 or 3 is pursued. One key exception to this is in respect of possible increased costs arising from litigation.

45. A central issue in considering implementation measures has been the possibility of increased litigation in the takeover regulatory field as a consequence of a change in the legislative regime. The very existence of the Directive creates a legislative environment which did not exist previously. It also introduces, inevitably, the possibility of new legal considerations and challenges, and the associated costs. Litigation is undesirable as it both impedes the fluidity of the takeover market, undermining the certainty with which a bidder can proceed to launch a bid, and adds to the costs of any such bid. These costs are ultimately borne by the shareholders of the bidder and target companies.

46. Along with the Panel and others participating and advising in the takeover field, the Government has considered in detail the practical and legal implications of the various options for implementing the Directive. The Government has concluded that the most transparent, effective and legally certain means of proceeding is to place the activities of the Panel within a legislative framework. The Government has concluded that the additional costs arising from the new legislative and regulatory regime are not likely to be significant¹⁴.

47. Under option 3, it is considered that the possible litigation costs would be increased due to the additional legal uncertainties as to whether recognition of a non-statutory Code as applied by a non-statutory body would constitute proper implementation of the Directive. There are, however, a number of provisions in the Interim Regulations and the Code which are intended to limited the threat of tactical litigation by: a) providing an opportunity for parties to seek rulings from the Panel (and, if unresolved, from the Panel's Hearings Committee and the independent Takeover Appeal Board); b.) excluding new rights of action for breach of statutory duty; (c) protecting concluded transactions from challenge for breach of the Panel's rules; and (d) exempting the Panel and its individual members, officers and staff from liability in damages for things done in, or in connection with, the discharge of regulatory functions of the Panel.

New Disclosure Requirements

48. New disclosure requirements will be imposed on all companies with shares that are admitted to trading on a regulated market under article 10 of the Directive. Under Regulation 26 of the Interim Regulations, companies will be required to include various facts and figures relating to the control and structure of their shares in their directors' reports and to make a report to their shareholders at the company's annual general meeting.

49. All of the information required by Regulation 26 will be readily known to companies (or at least be accessible) and some is likely already to be included in directors' reports. However, it is unlikely that any company would presently make a report on such information to its shareholders, as required by article 10(3). It therefore follows that the principal cost will be staff time in:

- initially researching and preparing the information in the format

¹⁴ In the consultation paper published by the Panel on 18 November 2005 ("The Panel on Takeovers and Mergers - The Implementation of the Takeovers Directive – Proposals Relating to Amendments to the Code", the Panel stated, paragraph 2.4, "Overall, the Panel remains confident that while its status and the status of the Code will be different under the new statutory regime, there will be little material substantive change either to its procedures or the Rules of the Code. As a result, the practical, day-to-day impact of the legislative changes will be small and the Panel's relationship with its regulated community will be largely unaffected. The Panel will continue to regulate takeover activity in the UK with a flexible approach, offering speed, and certainty in decision-making and seeking to ensure compliance with the Code through consensus with the parties involved".

required by the Directive;

- updating it as and when necessary;
- drafting the report(s).

50. It seems unlikely that the costs of producing and printing the directors' report will increase as a result of the new article 10 requirements.

51. The amount of time that will be taken up preparing the information and drafting the report will clearly vary from company to company. However, if it is assumed that a manager would spend between four and eight hours on this work the cost would be, approximately, between £100 and £200¹⁵. It seems likely that most companies would seek the opinion of a solicitor on the information set out in the directors' report (most companies will, in any case, employ a solicitor to consider their annual reports prior to publication) and if it is assumed that a solicitor would spend between one and two hours considering the information the cost would be, approximately, between £300 and £600¹⁶.

52. Accordingly, the cost per company of complying with article 10 would, on the above basis, be between £400 and £800. However, due to the interim nature of the Regulations, the vast majority of companies will not be required to report under the Interim Regulations prior to their repeal as they will not complete a reporting year during this period.

53. It is also possible that some costs might be offset by the increased ease of access to information on share and control structures on companies elsewhere within the EU and from wider benefits to a company arising from review of the appropriateness of its corporate structures.

Costs – Environmental and Social

54. The Directive would appear not to impose any environmental or social costs.

Equity and Fairness

55. The Directive (and, therefore, the Interim Regulations) apply only to companies whose shares are admitted to trading on a regulated market. It is estimated that there are 1,700 such companies. All other public companies (i.e. 11,300 of the total of 13,000 public companies) will not be affected by the new statutory regime during the period for which the Interim Regulations are in force.

¹⁵ In 2003, the average hourly pay, excluding overtime, of a manager/senior official in Great Britain was £19.28. The cost of a manager's time, including non-wage costs and overheads is estimated at 30% of wage costs. The hourly cost of a manager's time is, therefore, £19.28 x 1.3 = £25.06. Source: New Earnings Survey (NES) 2003.

¹⁶ This is based on a rough estimate of hourly fees of £300 (excluding VAT).

56. The Interim Regulations and the Code apply to private companies only in very limited circumstances. Accordingly, they will not affect the 2.1m GB registered private companies.

Consultation with Small Business: the Small Firms' Impact Test

57. The Interim Regulations will have limited effect on small firms since they apply only to companies whose shares are admitted to trading on a regulated market. Those companies to which this requirement applies will for the most part have shares listed on the London Stock Exchange. It is a requirement of the Financial Services Authority's Listing Rules that no company may list on the London Stock Exchange unless it has a minimum share capital of £700,000. Most small businesses will be private companies or sole traders and, even though some will be public companies, none will have a share capital of £700,000.

Competition Assessment

58. Implementation of the Directive will affect all markets since takeovers are not restricted to any particular sector. It is not anticipated that the costs of the Interim Regulations will affect some firms substantially more than others, nor that the Interim Regulations will lead to higher set-up costs or ongoing costs for new or potential firms that existing firms will not have to meet. Implementation of the Directive will not restrict the ability of firms to choose the price, quality, range or location of their products.

59. Implementation of the Directive, in itself, is not likely to affect market structure in the UK, i.e. it will not change the number or size of firms. Whilst takeovers clearly result in a change to the numbers and size of companies, it is not anticipated that the Interim Regulations will have any effect on takeovers of UK companies, i.e. companies will not be encouraged or discouraged by the Directive to embark on takeovers of UK companies. However, it is possible that the Directive may result in more takeovers by UK companies of companies in other EU States due to the implementation of common rules across the EU, even on a minimum standards basis. It is not anticipated that the Directive will affect competition, either positively or negatively, in UK. **This matter cannot, however, be influenced by the Interim Regulations.**

Enforcement and Sanctions

60. The Panel will be responsible for enforcing the rules contained in the Code. The Panel will have power to order compensation in circumstances where a rule requiring the payment of money has been breached and to apply to the court to enforce its rulings and directions. The Panel will also be able to impose a range of sanctions upon persons who breach its rules, including reporting conduct to other regulatory authorities, such as the Financial Services Authority.

61. The Panel's rules are presently enforced largely without the availability of statutory powers or sanctions. Notwithstanding the relative informality of the Panel's existing powers and sanctions, a high level of compliance with the Code and the rulings of the Panel has been attained. The absence of formality has been seen as a strength of the Panel in achieving speed in decision making and a good degree of openness from those involved in the takeover bid process. It is intended that the new statutory powers to be given to the Panel should not undermine the benefits of this approach to regulation which the Panel will continue to promote.

62. The Department of Trade and Industry (the Department of Enterprise, Trade and Investment for Northern Ireland) will be responsible for enforcement of other provisions in the Interim Regulations, including the new criminal offences created in connection with unlawful disclosure of information subject to secrecy provisions, bid documentation which fails to meet the standards required by the Directive and where a company fails to notify relevant takeover authorities of its decision to opt-in or out of article 11 of the Directive (relating to matters such as the types of restrictions in a company's articles or in contractual agreements that may apply in a takeover situation).

Monitoring and Review

63. Article 20 of the Directive provides that the Commission shall, in 2011, examine the Directive in the light of experience and, if necessary, propose its revision. The examination is to include a survey of the control structures and barriers to takeover bids that are not covered by the Directive. To help the Commission with its examination, article 20 requires Member States to provide the Commission annually with detailed information relating to takeover activity. DTI and the Panel will also keep the implementation of the Directive under review.

64. In view of the interim nature of the Regulations, however, it is not proposed to formally review their operation. The provisions of the Company Law Reform Bill, which will supercede the Interim Regulations, will be reviewed as part of the review process related to provisions in that Bill.

Consultation

Within Government

65. DTI consulted widely within Government including the Cabinet Office, Department for Constitutional Affairs, HM Treasury and Department of Enterprise, Trade and Investment (Northern Ireland) as well as the Financial Services Authority and Small Business Service in preparing the provisions to implement the Directive now contained in the Company Law Reform Bill, on which the Interim Regulations are substantially based.

Public Consultation

66. Extensive consultation has been undertaken by DTI, both during the negotiation of the Directive and in preparing for its implementation. This included:-

- “City Group” of key business and City consultees set up to advise on negotiation of the of the Directive;
- Informal meetings with consultees prior to publication of consultation document on implementation of the Directive (autumn 2004);
- Public consultation document (including draft Regulatory Impact Assessment)¹⁷ January 2005; and
- Government Response to the public consultation exercise and draft clauses for inclusion in the Company Law Reform Bill published on 17 July 2005¹⁸.

67. In particular, there were 23 responses to the January 2005 public consultation document. These responses indicated that there was:-

- consensus that the Panel should remain the takeover regulatory authority, retaining substantial autonomy and independence;
- provisions on “tactical litigation” should seek to restrict the opportunities of target companies to utilise tactical litigation to frustrate takeover bids – whilst ensuring that decisions of the Panel remain subject to appropriate appeal processes and the right for applicants to seek judicial review in appropriate circumstances; and
- as regards the provisions of the Directive relating to barriers to takeovers (articles 9, 11 and 12), legal effect should be given to the existing approach in the Code that the management of a target company should not take action to frustrate a takeover bid without the approval of shareholders at the time of the bid. Similarly, the large majority of consultees considered that a Member State option under the Directive should be exercised to maintain existing contractual freedoms under UK law for companies to establish such share and control structures as they choose.

68. The approach advocated by consultees on these issues has been followed in the Interim Regulations (and in Part 22 of the Company Law Reform Bill which will replace the Interim Regulations). Guidance on the interim regime to be given effect to by the Interim Regulations together with a draft of the instrument

¹⁷ “DTI – Company Law – Implementation of the European Directive on Takeover Bids – A Consultative Document” (January 2005, DTI/Pub 7710/0.8k/01/05/NP URN 05/511 (available on the DTI website: <http://www.dti.gov.uk/cld/currentcondocs.htm>).

¹⁸ “DTI – Company Law – Implementation of the European Directive on Takeover Bids - Government Response and Summary of Responses to the Consultative Document” together with draft clauses available on the DTI website <http://www.dti.gov.uk/cld/clauses.htm>

were placed on the website of the Department of Trade and Industry in March 2006¹⁹.

69. Additionally, in November 2005, the Panel published a full public consultation document²⁰ on the changes necessary to make the rules in the Code wholly consistent with the requirements of the Directive. Those changes, amended in the light of consultation, were adopted by the Code Committee of the Panel on 11 April 2006. A full response statement to the consultation exercise, setting out all the changes, was published by the Panel on 21 April 2006. The Code adopted by this instrument includes those changes. The Code, and all the changes made, are available on the Panel's website. A new edition of the Code, incorporating all the changes, will be published shortly before 20 May 2006.

Summary and Recommendation

70. Action is required to implement the Directive. The responses to the January 2005 consultative document supported the proposal that this be achieved through delegated statutory powers being given to the Panel. That avenue of implementation is currently being taken forward through the Company Law Reform Bill.

71. The Bill will not, however, have completed Parliamentary passage prior to 20 May 2006, by when the Directive must be implemented. There are only two possible means of implementing the Directive during the interim period:-

- *Option 2 – Direct Statutory Provision*
- *Option 3 – Give Recognition to the Takeover Code*

72. It is considered that both of these options are unlikely to involve significant costs to business, and carry some potential benefits in terms of the wider EU Single Market. However, in view of the additional legal uncertainties involved in giving recognition to the Code, the view is taken that interim implementation should be undertaken by direct statutory provision being made in the Interim Regulations.

¹⁹ "Implementation of the EU Directive on Takeover Bids - Guidance on changes to the rules on company takeovers" available on DTI website: <http://www.dti.gov.uk/cld/hottopics.htm>.

²⁰ A copy of the consultation paper, "The Implementation of the Takeovers Directive – Proposals relating to amendments to the Takeovers Code", is available on the Panel's website <http://www.thetakeoverpanel.org.uk/new/>. The consultation closed on 10 February 2006.

Declaration

73. I have read the Regulatory Impact Assessment and I am satisfied that the benefits justify the costs

Gerry Sutcliffe

Parliamentary Under-Secretary of State (Minister for Employment Relations and Consumer Affairs)

Dated 25th April 2006

Contact Point

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ANNEX – SUMMARY OF RISKS, BENEFITS AND COSTS OF OPTION 2 AND 3

	Option 2 – Direct Statutory Provision	Option 3 – Give recognition to the Code
BENEFITS OF THE DIRECTIVE AS IMPLEMENTED BY THE INTERIM REGULATIONS (those items marked with an asterisk indicate that there are no, or insignificant, benefits arising to domestic takeover regulation)		
* Encouragement of takeover bid activity through common rules in EU	Yes	Yes
* EU mandatory bid rule	Yes	Yes
* EU equitable price rule	Yes	Yes
Increased transparency and disclosure by EU companies traded on a regulated market	Yes	Yes
* Restrictions on frustrating action by management of target company	Yes (but only on voluntary basis for Member States/companies)	Yes (but only on voluntary basis for Member States/companies)
* EU Squeeze-out and sell-out rules	Yes	Yes
COSTS OF THE DIRECTIVE AS IMPLEMENTED BY THE INTERIM REGULATIONS (the item marked with an asterisk indicates that these are not costs that could be affected by the implementing Interim Regulations)		
* Two tier regime of takeover regulation – applying differently to transactions falling within the scope of the Directive from those falling outside of it	Yes	Yes
Increased likelihood of tactical litigation	Considered this issue is satisfactorily addressed	Yes
Costs of additional disclosure requirements for companies	Yes (between £400 and £800 per company where the requirement applies)	Yes (between £400 and £800 per company where the requirement applies)
RISKS OF THE DIRECTIVE AS IMPLEMENTED BY THE INTERIM		

REGULATIONS (those items marked with an asterisk indicate that they are not risks that could be affected by the implementing Interim Regulations)		
Positive (leading to more open takeover markets and increased competition):-		
Improved shareholder protection	Yes	Yes
Improved access to capital markets	Yes	Yes
Convergence of takeover regulatory regimes as a consequence of “soft-harmonisation”	Yes	Yes
Adverse (leading to more restricted takeover markets and less competition):-		
* Minimum standards approach of the Directive	Yes	Yes
* Main barriers to takeovers articles are not mandatory for EU Member States	Yes	Yes
More prescriptive and litigation driven approach to takeover regulation in UK	Considered this issue is satisfactorily addressed	Yes
* Companies choosing to move share listing from regulated markets	Yes	Yes
* Non-legal/regulatory factors restricting takeover activity not addressed	Yes	Yes

TRANSPOSITION NOTES

DIRECTIVE 2004/25/EC OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL OF 21 APRIL 2004 ON TAKEOVER BIDS

The Takeovers Directive (Interim Implementation) Regulations 2006

1. The Takeovers Directive (Interim Implementation) Regulations 2006 (the “Regulations”) implement within the UK Directive 2004/25 EC of the European Parliament and of the Council of 21 April 2004 on Takeover Bids (OJ L142, 30 April 2004) (“Takeovers Directive”). The Takeovers Directive must be implemented by 20 May 2006.
2. Provisions substantively implementing the Takeovers Directive are contained in the Company Law Reform Bill (the “Bill”), which is presently being considered by Parliament. However, the Bill will not have completed Parliamentary passage and received Royal Assent prior to 20 May 2006. Accordingly, the Regulations, which have been made under section 2(2) of the European Communities Act 1972 (the “1972 Act”), implement the Takeovers Directive on an interim basis pending the coming into force of the relevant provisions in the Bill (it is the intention that the Regulations will be repealed at that time). The provisions in the Regulations are closely modelled on the provisions to implement the Takeovers Directive contained in the Bill, with certain key differences reflecting limitations imposed by the 1972 Act.
3. The Takeovers Directive lays down, for the first time, minimum EU rules concerning the regulation of takeovers of companies whose shares are traded on a regulated market. The Takeovers Directive was one of the measures adopted under the EU Financial Services Action Plan and aims to strengthen the Single Market in financial services by facilitating cross-border restructuring and enhancing minority shareholder protection.
4. The Takeovers Directive contains general principles that Member States must adhere to in regulating takeover activity and a framework relating to the functions and jurisdiction of takeover regulatory authorities. It also lays down provisions relating to the mandatory bid (a requirement whereby a party gaining control of a company must make an offer to all shareholders at an equitable price), takeover bid documentation, time allowed for acceptance of the bid, the obligations of the board of the offeree company and other matters related to the bid.
5. Additionally, the Takeovers Directive has provisions addressing barriers to takeovers (such as action that might be taken by a company or its board before or during a bid to prevent a takeover), requiring disclosure of certain information by companies traded on a regulated market and dealing with the problems of, and for, residual minority shareholders following a successful takeover bid (so-called ‘squeeze-out’ and ‘sell-out’ provisions).
6. Since 1968, takeover regulation in the United Kingdom has been overseen by the Panel on Takeovers and Mergers (“the Panel”) enforcing rules and principles contained in The City Code on Takeovers and Mergers. In order to bring UK takeover regulation within the requirements laid down in the Takeovers Directive, the Regulations are designed, for the first time, to place takeover regulatory functions within a complete and coherent statutory framework.

7. Provisions related to disclosures by companies are contained in Part 7 of the Companies Act 1985 (Part 8 of the Companies (Northern Ireland) Order 1986 in Northern Ireland). Those requirements are supplemented by additional disclosure requirements imposed by the Takeovers Directive on companies traded on a regulated market.

8. ‘Squeeze-out’ and ‘sell-out’ provisions are prescribed by Part 13A of the Companies Act 1985 (Part 14A of the Companies (Northern Ireland) Order 1986). These provisions have been adapted to ensure they are wholly consistent with the Takeovers Directive requirements and applied on a self-standing basis in relation to companies to which the Takeovers Directive applies.

9. The detailed rules relating to takeover regulation in compliance with the Takeovers Directive are set out in The City Code on Takeovers and Mergers and the Rules of Procedure of the Panel’s Hearings Committee (“the Code”) laid down by the Panel. The Panel have made changes to the Code (as it applies from 20 May 2006) necessary to make it wholly compliant with the Directive. The Regulations give effect to the rules of the Code for the purposes of the Takeovers Directive (see regulation 2 (Interpretation) and regulation 3 (The rules)). For the period the Regulations are in place, such rules can only be altered through supplemental Regulations made under the 1972 Act.

10. Responsibility for the measures, described in this transposition note, taken to implement the Takeovers Directive lies with the Secretary of State for Trade and Industry.

11. The table below describes the substantive provisions implementing the Takeovers Directive.

Part 22: Takeovers etc: Transposition Measures		
Article	Objective	Implementation
1	Defines the scope of the Directive in terms of transactions and types of company to which it applies (“takeover bids for the securities of companies governed by the laws of Member States, where all or some of those securities are admitted to trading on a regulated market”).	No specific implementing provision necessary.
2	Contains key definitions for the purposes of the Directive (such as, “takeover bid”, “offeree company”, and “securities”).	No specific implementing provision necessary.
3.1	Lays down general principles which Member States shall ensure are adhered to for the purpose of implementing the Directive.	The General Principles section of the Code sets out in identical terms the general principles laid down in the Takeovers Directive.
3.2	Provides that Member States, with a view to ensuring compliance with the general principles, must ensure that the minimum requirements set out in the Directive are observed and may lay down additional	No specific implementing provision necessary.

	conditions and provisions more stringent than those of the Directive.	
4.1	Requires Member States to designate supervisory authorities (which must act independently of parties to a bid).	Regulation 4 designates the Panel to supervise takeover bids to which the Directive applies.
4.2	Lays down jurisdictional rules in relation to takeover regulation (this includes “split jurisdiction” cases” i.e. a company that is registered in one Member State, but whose shares are traded on a regulated market in another Member State).	The jurisdictional provisions relating to the takeover bids which will be supervised by the Panel, are laid down by section 3 of the Introduction to the Code.
4.3	Requires Member States to ensure that persons employed or formerly employed by takeover regulatory authorities are bound by professional secrecy (information covered by this obligation should not be disclosed other than under conditions laid down by national law).	Regulation 8 makes it a criminal offence to disclose information provided to the Panel other than under the circumstances and through the gateways laid down in regulation 7 (and Schedule 1).
4.4	Lays down cooperation obligations in relation to EU takeover and financial markets supervisory authorities.	Regulation 9 imposes cooperation obligations on the Panel and the Financial Services Authority. Additionally, section 12 of the Introduction to the Code sets out the basis on which the Panel will effect service of documents on behalf of other regulatory authorities in accordance with the Directive provisions.
4.5	Requires that takeover supervisory authorities be provided with all powers necessary for carrying out their duties and provides that Member States may, provided that the general principles are respected, permit derogation from the rules of the Directive in certain circumstances and grant supervisory authorities the power to grant waivers.	<p>The following powers are provided to the Panel by the Regulations:</p> <ul style="list-style-type: none"> i. Regulation 2(2)(a)(i) – power to give directions in relation to rules in the Code; ii. Regulation 2(2)(a)(ii) – power to order the payment of compensation by a person in breach of a rule in the Code; iii. Regulation 2(2)(a)(iii) – power to impose sanctions on a person who has acted in breach of a rule in the Code or failed to comply with a direction; iv. Regulation 2(2)(b) – power for decisions of the Panel to be reviewed by a committee of the Panel and for a decision of that committee to be appealed to an independent tribunal; v. Regulation 2(2)(c) – power to require fees or charges to be payable to the Panel for the purpose of meeting its expenses; vi. Regulation 2(2)(f) and (g) – power to make rulings in relation to rules in the Code and for those rulings to have binding effect; vii. Regulation 6 - power to require documents and information;

		<p>viii. Regulation 11– power to apply to the court for enforcement; and</p> <p>ix. Regulation 15 – power to bring and defend proceedings.</p> <p>Regulation 2(2)(d) authorises the Panel to enforce rules subject to exceptions or exemptions and regulation 2(2)(e) authorises it to dispense with or modify the application of rules in the Code in particular cases. Circumstances in which the Panel may give derogations or grant waivers are set out in section 2(c) of the Introduction to the Code.</p>
4.6	<p>Makes provision for certain Member States’ powers to be unaffected by the Directive (for instance, designation of judicial or other authorities responsible for dealing with disputes, the circumstances in which parties may bring administrative or judicial proceedings, any capacity of the courts to decline to hear legal proceedings and the liability of supervisory authorities).</p>	<p>Matters related to hearings in respect of Panel decisions are contained in the Code.</p> <p>In particular:-</p> <p>i.) Section 7 of the Introduction to the Code explains the role of the Hearings Committee of the Panel (dealing with matters such as hearings before the Committee, time limits, frivolous or vexatious applications, procedural rulings and the right of appeal);</p> <p>ii.) The Rules of Procedure of the Hearings Committee includes matters such as the composition of the Committee, the role of the Chairman and the powers of the Committee;</p> <p>iii.) Section 8 of the Introduction to the Code deals with the role of the independent Takeover Appeal Board (this Board will maintain its own rules of procedure made under common law powers).</p> <p>Regulation 12 provides that there shall be no action for breach of statutory duty, etc. in relation to a rule-based requirement (under the Code) or a disclosure requirement under regulation 6, and that contravention of a rule-based requirement does not make any transaction void or unenforceable or affect the validity of any other thing.</p> <p>Regulation 16 provides for exemption of the Panel (and those involved in its functions) from liability in damages in certain circumstances related to the regulatory activities of the Panel.</p>
5	<p>Requires that a “mandatory bid rule” is introduced requiring a person acquiring “control” of a company to make a bid to all holders of securities at an equitable price</p>	<p>Rule 9 of the Code requires that a mandatory bid be made to all shareholders where a person acquires 30% or more of the voting rights in a company.</p>

	Contains rules related to the calculation of the equitable price.	Equitable price rules are set out in Rule 9.5 of the Code.
6	<p>Requires that the decision to make a takeover bid is made public and that the supervisory authorities and employee representatives or employees are informed.</p> <p>Requires that an offer document is drawn up and made public and that it is communicated to the supervisory authority and the employee representatives or employees.</p> <p>Contains detailed provision related to the contents of the offer document.</p> <p>Requires that the parties to a bid are obliged to provide supervisory authorities with information related to the bid.</p>	<p>Rule 2 of the Code sets out these provisions.</p> <p>Rules 30 and 32 of the Code set out these provisions.</p> <p>Rule 24 and 27 of the Code specify what must be contained in the offer document and Regulation 10 makes it a criminal offence to fail to comply with those rules to the extent that they are referred to in section 10(e) of the Introduction to the Code.</p> <p>Regulation 6 provides the Panel with power to require documents and information.</p>
7	Lays down rules related to the time allowed for acceptance of the takeover bid.	Rule 31 of the Code lays down rules concerning the bid timetable.
8	<p>Requires that takeover bids are made public so as to ensure market transparency.</p> <p>It also provides for the disclosure of bid documentation to shareholders and employee representatives or employees.</p>	<p>Rule 2 sets out these provisions.</p> <p>Rules 25, 30 and 32 of the Code provide for disclosure of bid documentation to shareholders and employee representatives or employees.</p>
9	Imposes obligations on the board of the offeree company, including the obligation not to take action to frustrate the bid without the approval of shareholders at the time of the bid and to draw up and make public a document containing their views on the effects of implementation of the bid and communicate it to the employee representatives or employees (and append the opinion of employee representatives, if it is received in good time).	<p>Rule 21 of the Code lays down provisions preventing action being taken by the management of an offeree company, without the agreement of shareholders at the time of the bid, to frustrate a takeover bid.</p> <p>Rules 25, 27, 30 and 32 of the Code require the board of the offeree company to prepare and issue a statement setting out its opinion on the bid and Regulation 10 makes it a criminal offence to fail to comply with rules 25 and 27 to the extent that they are referred to in section 10(e) of the Introduction to the Code.</p> <p>Rules 30 and 32 also set out the provisions in relation to employee representatives/employees.</p>

10	Requires that companies shall publish detailed information on their share and control structures, etc. in their annual report and present an explanatory report on such matters to the annual general meeting of shareholders.	Part 4 of the Regulations requires that the relevant information, including necessary explanatory material, is set out in the directors' report of those companies covered by the Directive.
11	“Breakthrough” – This provision overrides, in certain circumstances connected with a takeover, provisions in the articles of companies and contractual arrangements related to restrictions on transfer and voting rights of shares, etc. It does not apply to special shares held by Member States or to cooperatives.	Regulation 20(3) excludes the right to opt-in to “breakthrough” provisions where the articles of association contain restrictions that are prohibited by article 11. Regulation 22 lays down the effect on contractual restrictions overridden by “breakthrough”.
12.1	Provides that Member States may make optional the provisions of articles 9(2) and (3) and/or article 11.	Exercise of this option has been taken only in relation to the provisions of article 11 . Regulations 20 and 21 define the types of companies, circumstances and mechanisms by which a company may opt-in.
12.2 (and 12.4)	Requires, where optional arrangements are in place, that companies have the right voluntarily to opt-in to the provisions of the relevant articles. Such a decision must be communicated to the supervisory authorities and be disclosed.	Regulation 20 entitles a company to choose to opt-in to the provisions of Article 11 of the Directive. Regulation 24 requires that any opting-in decision be communicated to the Panel without delay. By virtue of it being a special resolution, the opting-in resolution passed by the company must be filed with the Registrar of Companies under section 380 of the Companies Act 1985 (or, as the case may be, Article 388 of the Companies (Northern Ireland) Order 1986).
12.3 (and 12.5)	Permits Member States to provide that the effects of articles 9(2) and (3) and/or article 11 only apply on a “reciprocal” basis, i.e. where the takeover bid is made by a company also subject to the effects of the relevant articles. Such restrictions on the application of articles 9(2) and (3) and/or article 11 shall be subject to the authorisation of the general meeting of shareholders of the offeree company.	The Member State option to provide for “reciprocity” has not been exercised.
13	Requires that rules relating to the following be put in place:- a.) the lapsing of bids;	There are a large number of Rules in the Code which deal with these issues. These include the following:- a.)Rule 12.1 (lapse in event of reference to Competition Commission), Rule 31 (rules related to final day of the bid and time for fulfilment of conditions), Rule 35.4 (restrictions on dealings by a competing

	<p>b.) the revision of bids;</p> <p>c.) competing bids;</p> <p>d.) the disclosure of the results of bids; and</p> <p>e.) the irrevocability of bids and the conditions permitted.</p> <p>These provisions do not include detailed requirements as to the contents of such rules.</p>	<p>offeror whose offer has lapsed)</p> <p>b.) Rule 32 (revision of bids)</p> <p>c.) Rule 20.2 (equality of information on competing bids), Rule 32.5 (competitive situations)</p> <p>d.) Rule 31.6(c) (final day rule (fulfilment of acceptance condition, timing and announcement))</p> <p>e.) Rule 2.5 (consequences of an announcement and subjective conditions), Rule 9.3 (conditions permitted in a mandatory bid), Rule 13 (subjective conditions) and Rule 34 (Right of withdrawal)</p>
14	Provides that the Directive shall be without prejudice to various provisions relating to information and consultation of employees and their representatives.	No specific implementing provision necessary.
15	<p>Requires Member States to put in place rules enabling a bidder to compulsorily purchase the shares of minority shareholders following a successful takeover bid (“squeeze-out” rights).</p> <p>The circumstances in which such a right must apply (including time periods and relevant thresholds) and relating to the price that must be paid are set out.</p>	<p>“Squeeze-out” rights and related provisions are contained in Part 5 of the Regulations, in particular in paragraphs 1, 2, 3 and 6 to 10 of schedule 2.</p> <p>These provisions are consistent with the time periods, relevant thresholds and other provisions laid down by the Directive.</p>
16	<p>Requires Member States to put in place rules enabling minority shareholders to require a bidder to compulsorily purchase their shares following a successful takeover bid (“sell-out” rights).</p> <p>The circumstances in which such a rule must apply (including time periods and relevant thresholds) and relating to the price that must be paid are set out.</p>	<p>“Sell-out” rights and related provisions are contained in Part 5 of the Regulations, in particular in paragraphs 1, 4, 5 and 6 to 10 of schedule 2.</p> <p>These provisions are consistent with the time periods, relevant thresholds and other provisions laid down by the Directive.</p>
17	Requires that effective, proportionate and dissuasive sanctions be put in place.	<p>Section 11 of the Introduction to the Code sets out the disciplinary powers of the Takeover Panel and the sanctions and other remedies available for breach of the Code.</p> <p>Section 10(c) of the Introduction to the Code sets out the circumstances in which the Panel may order compensation to be paid.</p> <p>Regulation 8 makes it an offence to contravene the provisions of regulation 7 (relating to the restrictions on disclosure of</p>

		<p>information provided to the Panel).</p> <p>Regulation 10 provides an offence where takeover bid documentation does not comply with rules 24, 25 and 27 of the Code to the extent that they are referred to in section 10(e) of the Introduction to the Code concerning “offer” documents (prepared by the bidder) and “response” documents (from the management of the offeree company).</p> <p>Paragraphs 2(10) and 4(12) of Schedule 2 provide for offences where the offeror fails to notify minority shareholders of its intention to acquire their shares and of their right to require their shares to be acquired.</p> <p>Misconduct in relation to takeover activity also needs to be viewed in the wider context of the overall regulatory framework and the protections available to shareholders and others.</p> <p>A robust market regulatory regime and company law framework is in place in the United Kingdom to investigate and pursue misconduct in relation to takeover activity (for instance, stringent sanctions are already in place to deter fraudulent misrepresentation or market abuse).</p>
18	Lays down a Committee procedure whereby the Commission may adopt rules related to the application of article 6.3 (contents of takeover bid documentation).	No implementing provision necessary (no such rules have been adopted).
19	Requires the EU Commission to establish a Contact Committee to facilitate the harmonised application of the Directive and advise the Commission, if necessary, on any additions or amendments to the Directive.	No implementing provision necessary.
20	<p>Provides for the review of the Directive by the EU Commission five years after its entry into force.</p> <p>Requires that Member States provide the Commission annually with certain information related to takeover bids.</p>	<p>No implementing provision necessary.</p> <p>Such information will be provided to the EU Commission as an administrative process.</p>
21	Requires that the relevant provisions of the Directive be transposed no later than 20 May 2006. Details of transposition measures shall be communicated to the Commission.	No specific implementing provision necessary. Details of the transposition measures will be communicated to the EU Commission by administrative process.
22	Provides that the Directive enters into force on 20 May 2004.	No implementing provision necessary.
23	Addresses the Directive to the Member States.	No implementing provision necessary.

