

European Directive on Takeover Bids

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Structure of the Presentation

- I. Background to the adoption of the Directive
- II. Main Provisions of the Directive

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Introduction

- The harmonisation of European takeover regulations: a *sine qua non* for the creation of an integrated capital market by 2010.
- First attempts to harmonise takeover law in Europe
- The Commission's 1985 White Paper on completing the internal market
- An initial proposal for a Directive on takeover bids (also known as the Thirteenth Directive on company law) presented by the Commission on 19 January 1989
- Adoption of an amended proposal the next year. This proposal encountered strong opposition and was withdrawn in 1991.
- Drafting of a less ambitious proposal on 8 February 1996: a so-called "framework Directive", which contained general principles. This proposal was approved by the Parliament by a large majority. The Commission transmitted to the Council and Parliament on 11 November 1997 an amended proposal for a Directive, which incorporated most of the amendments proposed by the Parliament.

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Introduction (cont'd)

- 2001: the compromise text failed to reach the necessary majority vote at the Parliament by one vote.
- September 2001: setting up of a High Level Working Group of Company Law Experts, chaired by Jaap Winter, to advise the Commission on the draft directive.
- January 2002: the Group issued its report and suggested that any European company law regulation aimed at creating a level playing field should be guided by two principles, namely **shareholder decision-making and proportionality between risk bearing and control**.
- 2 October 2002: new proposal by the Commission, which incorporated some of the recommendations made by the Group of High-Level Company Law Experts. The new proposal opted for a modified "mini" break through rule.
- Only a few weeks from completion of the political process, Germany shifted its position to oppose the Directive.
- A compromise text was tabled by Italy, which not only allowed MS to choose whether or not to implement the neutrality and/or the breakthrough rule, but also included reciprocity provisions. The proposal was adopted on that basis on 27 November 2003.

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Current Framework of the Directive

- A framework Directive establishing general principles governing takeovers without attempting detailed harmonisation.
- Thus, MS may lay down additional conditions and provisions more stringent than those of the Directive for the regulation of bids (**Art. 3.2(b)**)
- The Directive applies to both mandatory and voluntary takeover bids for transferable securities with voting rights of companies governed by the laws of a MS, where all or some of such securities are admitted to trading on a regulated market in one or more MS.

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Main Provisions of the Directive

Article 9:the neutrality rule

Article 11:the break through rule

Article 12.1:optional arrangements

Article 12.3:the reciprocity rule

Article 5:the mandatory bid rule

Articles 15-16:the right of squeeze-out and the right of sell-out

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Article 9: Neutrality Rule

- Different views as to the role of the offeree board in the face of a bid: managerial resistance view v. managerial passivity view
- Managerial passivity view: agency problem between the management of the offeree company and the offeree shareholders
- **Article 9.2:** *Once a bid has been made public, "the board of the offeree company shall obtain the prior authorisation of the general meeting of shareholders given for this purpose before taking any action, other than seeking alternative bids, which may result in the frustration of the bid and in particular before issuing any shares which may result in a lasting impediment to the offeror's acquiring control of the offeree company".*
- **Article 9.3:** *"As regards decisions taken before the beginning of the bid period and not yet partly or fully implemented, the general meeting of shareholders shall approve or confirm any decision which does not form part of the normal course of the company's business and the implementation of which may result in the frustration of the bid".*
- Sharp contrast with the US view of the board (managerial resistance view)
- However, the potential effects of the neutrality rule are muted out by the optionality rule.

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Article 11: Break Through Rule

- **Article 11.2:** *"Any restrictions on the transfer of securities provided for in the articles of association of the offeree company shall not apply vis-à-vis the offeror during the time allowed for acceptance of the bid".*
"Any restrictions on the transfer of securities provided for in contractual agreements between the offeree company and holders of its securities, or in contractual agreements between holders of the offeree company's securities entered into after the adoption of this Directive, shall not apply vis-à-vis the offeror during the time allowed for acceptance of the bid".
- **Article 11.3:** *"Restrictions on voting rights provided for in the articles of association of the offeree company shall not have effect at the general meeting of shareholders which decides on any defensive measures in accordance with Article 9".*
"Restrictions on voting rights provided for in contractual agreements between the offeree company and holders of its securities, or in contractual agreements between holders of the offeree company's securities entered into after the adoption of this Directive, shall not have effect at the general meeting of shareholders which decides on any defensive measures in accordance with Article 9".
"Multiple-vote securities shall carry only one vote each at the general meeting of shareholders which decides on any defensive measures in accordance with Article 9".

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Article 11: Break Through Rule (cont'd)

- **Article 11.4:** *“Where, following a bid, the offeror holds 75 % or more of the capital carrying voting rights, no restrictions on the transfer of securities or on voting rights nor any extraordinary rights of shareholders concerning the appointment or removal of board members provided for in the articles of association of the offeree company shall apply; multiple-vote securities shall carry only one vote each at the first general meeting of shareholders following closure of the bid, called by the offeror in order to amend the articles of association or to remove or appoint board members”.*
- However, the potential effects of the break through rule are muted out by the optionality rule.

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Article 12.1: Optional Arrangements

- *“Member States may reserve the right not to require companies [...] which have their registered offices within their territories to apply Article 9(2) and (3) and/or Article 11”.*
- However, the Directive requires MS who make use of the option to nevertheless grant companies which have their registered offices within their territories the option, which shall be reversible, of applying Article 9(2) and (3) and/or Article 11.

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Outcome of the Optionality Rule

Articles 9, 11 and 12 of the Directive together set forth a pro-takeover default system that MS can reverse

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Article 12.3: Reciprocity Rule

“Member States may exempt companies which apply Article 9(2) and (3) and/or Article 11 from applying Article 9(2) and (3) and/or Article 11 if they become the subject of an offer launched by a company which does not apply the same Articles as they do, or by a company controlled, directly or indirectly, by the latter”

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Overview of the Implementation of the Neutrality and the Break Through Rules across EU MS

Portier (2007) distinguishes four groups of MS:

1. The "French solution": France, Spain, Portugal, Slovenia, Greece, Cyprus and Hungary. This group opted into Article 9 and the corresponding reciprocity rule but opted out of Article 11.
2. The "British solution": the UK, Ireland, Austria, Tcheque Republic, Sweden, Finland, Slovaquia and Malte. This group opted into Article 9 but opted out of the corresponding reciprocity rule. They also opted out of Article 11.
3. The "Germanique group": Germany, Denmark, the Netherlands, Luxembourg, Poland, Belgium and Italy. This group opted out of both Articles 9 and 11.
4. The "Baltic group": this group opted into both Articles 9 and 11, without availing themselves of the reciprocity rule.

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Overview of the Implementation of the Neutrality and the Break Through Rules Across EU MS

MEMBER STATES	NEUTRALITY RULE	BREAK THROUGH RULE	RECIPROCITY RULE
FRANCE	✓	X	✓
SPAIN	✓	X	✓
PORTUGAL	✓	X	✓
SLOVENIA	✓	X	✓
GREECE	✓	X	✓
CYPRUS	✓	X	✓
HUNGARY	✓	X	✓
UK	✓	X	X
IRELAND	✓	X	X
AUSTRIA	✓	X	X
TSCHEQUE REPUBLIC	✓	X	X
SWEDEN	✓	X	X
FINLAND	✓	X	X
SLOVAQUIA	✓	X	X
MALTE	✓	X	X
GERMANY	X	X	
DENMARK	X	X	
NETHERLANDS	X	X	
POLAND	X	X	
BELGIUM	X	X	
ITALY	X	X	
BALTIC GROUP	✓	✓	

Implementation of the Neutrality Rule in the UK and France

Both the UK and France have opted into the neutrality rule. However:

- ✓ Unlike the UK Takeovers Directive (Interim Implementation) Regulations 2006, the French law transposing the Directive into national law (: the Act 2006-387 of 31 March 2006 on takeover bids) allows companies to use the reciprocity exception rule. Thus, no shareholder approval is required if the offeror is not itself subject to the neutrality rule. The only requirement is that the measure that may be taken by the board during the bid must have been expressly authorised in relation to the possibility of a public offer by the GM of shareholders during 18 months preceding the date of the bid.
- ✓ In addition, the new French law allows for the issuance of share warrants (*bons Breton*)

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Implementation of the Break Through Rule in the UK and France

Both the UK and France have opted out of the break through rule. However:

- Both MS allow listed companies based in their jurisdictions to implement the break through rule on a voluntary basis.
- Pre-bid defences are rarely used in the UK, due to the large presence of institutional investors in UK listed companies.
- A mini-break through rule in France: no share transfer restrictions in the articles of association may be invoked against the offeror during the bid period. In addition, limitations on the number of voting rights a shareholder may exercise shall not be applicable in the first GM that follows a successful takeover bid, if the offeror has acquired more than two-thirds of the shares or voting rights **(AMF Regulation, Articles 231-43 to 231-45)**

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Article 5: Mandatory Bid Rule

- **Article 5.1:** *"Where a natural or legal person, as a result of his/her own acquisition or the acquisition by persons acting in concert with him/her, holds securities of a company which, added to any existing holdings of those securities of his/hers and the holdings of those securities of persons acting in concert with him/her, directly or indirectly give him/her a specified percentage of voting rights in that company, giving him/her control of that company, Member States shall ensure that such a person is required to make a bid as a means of protecting the minority shareholders of that company"*.
- **Article 5.4:** *"The highest price paid for the same securities by the offeror, or by persons acting in concert with him/her, over a period, to be determined by Member States, of not less than six months and not more than 12 before the bid period shall be regarded as the equitable price"* (the highest price requirement)

No requirement that the mandatory bid be in cash, except in two circumstances.

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Articles 15-16: Squeeze-out Right and Sell-out Right

- **Article 15.2 (squeeze-out right):** *"Member States shall ensure that an offeror is able to require all the holders of the remaining securities to sell him/her those securities at a fair price. Member States shall introduce that right in one of the following situations:*
(a) where the offeror holds securities representing not less than 90 % of the capital carrying voting rights and 90 % of the voting rights in the offeree company,
or
(b) where, following acceptance of the bid, he/she has acquired or has firmly contracted to acquire securities representing not less than 90 % of the offeree company's capital carrying voting rights and 90 % of the voting rights comprised in the bid.
In the case referred to in (a), Member States may set a higher threshold that may not, however, be higher than 95 % of the capital carrying voting rights and 95 % of the voting rights".
- **Article 15.5:** *"Member States shall ensure that a fair price is guaranteed"*.

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Articles 15-16: Squeeze-out Right and Sell-out Right (cont'd)

Article 16.2 (sell-out right): "Member States shall ensure that a holder of remaining securities is able to require the offeror to buy his/her securities from him/her at a fair price under the same circumstances as provided for in Article 15(2)".

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Final Words

- The optional nature of Articles 9 and 11 puts into question whether the ultimate outcome of the Directive will indeed be the promotion of an efficient pan-European market for corporate control
- Bolkenstein: the Directive had "*fallen victim to horse-trading and unholy alliances*".
- The Directive is, however, the best achievable compromise, given the differences in company law around the EU.
- Review in 2011

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Thank you for listening

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