THE TAKEOVER PANEL

Report on the Year ended 31st March, 1989.

MEMBERSHIP OF THE PANEL

The Lord Alexander of Weedon QC (Chairman)	Nominated by the Governor of the Bank of England
J. F. C. Hull (Deputy Chairman)	Nominated by the Governor of the Bank of England
Sir Philip Shelbourne (Deputy Chairman)	Nominated by the Governor of the Bank of England
Sir Austin Pearce	Nominated by the Governor of the Bank of England
T. J. Palmer	Chairman, Association of British Insurers
C. H. Black	Chairman, Association of Investment Trust Companies
The Hon. T. J. Manners	Nominated by the British Merchant Banking and Securities Houses Association
I. A. N. McIntosh	Chairman, Corporate Finance Committee, British Merchant Banking and Securities Houses Association
J. G. Quinton	Chairman, Committee of London and Scottish Bankers
M. G. Taylor	Nominated by the Confederation of British Industry
The Lord Elton	Chairman, Financial Intermediaries, Managers and Brokers Regulatory Association
P. E. Couse	President, Institute of Chartered Accountants in England and Wales
G. M. Nissen	Chairman, Investment Management Regulatory Organisation
D. H. Brydon	Nominated by the National Association of Pension Funds
S. M. Yassukovich	Chairman, The Securities Association
A. C. Hugh Smith	Chairman, The Stock Exchange
J. S. Fairbairn	Chairman, Unit Trust Association
The Lord Roskill	Chairman of the Appeal Committee of the Panel

THE PANEL EXECUTIVE

A. R. Beevor	Director General
P. R. Frazer T. P. Lee	Deputy Directors General
N. P. Hinton J. G. Doctor	Assistant Directors General
R. W. Godden A. S. Clark Miss S. M. Govier	Secretaries
J. R. St. J. Miller D. H. Spriddell R. Dobson C. J. Bailey Miss C. E. Hambro A. J. Strachan T. P. Kennedy Mrs. T. A. Scott	Assistant Secretaries

CHAIRMAN'S FOREWORD

This will be my last Report as Chairman of the Panel. It is less than three years since I took over from Sir Jasper Hollom and my tenure has been short by comparison with my distinguished predecessors. It has, however, not been without incident.

Many questions were in my mind when I came to the Panel. I particularly wanted to understand and assess the merits of the informality and flexibility with which the Panel has worked. I have been given plenty of opportunity to do so. From the many situations we have dealt with, three can be taken as illustrations. First, the Britoil case caused us to consider the impact of "golden shares" upon, amongst other things, the application of the principle of "majority rule" contained in the Code. Then there was the Irish Distillers case, which required us to consider the impact of EEC anti-trust law upon the Code timetable. Finally, and more recently, the interaction between law suits and the Code fell to be considered in connection with the offer by Minorco for Consolidated Gold Fields. In all these and other cases, the Code has had to be applied to novel situations. The Panel has approached its task in a flexible manner, giving weight to the spirit and purpose of the Code rather than merely its letter.

As a lawyer who has always been attracted by a purposive approach to law, I have become convinced of the fundamental necessity of dealing with takeovers in this way. What the Australians call "black letter law", which means that there is no discretion for a broad application of the principle of a rule, would be wholly inappropriate for an area of activity where ingenuity and financial dynamism lead to the evolution of new approaches and the emergence of novel issues. Flexibility is crucial, since otherwise there would be no way of dealing with these new problems. If the approach was more rigid, advisers would be legitimately free to design round the letter of the law to avoid its spirit.

Vital as flexibility is, however, it would lead to uncertainty, and consequent unfairness, if it were not for the ability of the Panel to give the parties to offers prompt and authoritative guidance and rulings as to the application of the Code to particular proposals in advance of those proposals being implemented. This enables the parties to know where they stand. It has the added benefit that the Panel can, by requiring advance consultation whenever there is any doubt as to the application of the Code, intervene to prevent undesirable actions occurring, rather than merely remedying breaches of the Code after the event. We lawyers are often involved in picking up the pieces when the damage is done. The system of dispute resolution which the Panel operates generally resolves the issue whilst it is live so that shareholders' interests get immediate protection and damage is prevented. It is positive and constructive.

During recent years, some attempts have been made to litigate the Panel's decisions. As a barrister, before joining the Panel, I argued the case for the Panel in the first of these cases, Datafin, in happy ignorance of the impact the decision would have on my future activities. The approach so skilfully and pragmatically laid down by the Court of Appeal seems to me to work well. The Courts have now held in three cases that they will not hold up takeovers by adjudicating during the course of a takeover on decisions taken by the Panel. They have shown themselves sensitively aware that litigants would otherwise make applications for tactical purposes to delay and possibly wholly to frustrate the conduct of the bid. There is a good deal of such litigation in the United States. It is wholly desirable that our Courts have set their face so firmly against going down the same route. If we have a system of alternative dispute resolution, logic and good sense dictate that it should be permitted to operate in accordance with the timetable governing the conduct of bids.

One provision of the Code which seems to me of critical importance is the "anti-frustration" rule. This avoids management taking action during a takeover, or when a takeover is imminent, which is designed to frustrate the bid. There is always a danger that management could confuse the interests of their company with the belief that their own continued involvement was necessarily crucial to the success of the company. It is important that in such a situation of potential conflict of interest, shareholders should be given the opportunity of considering whether or not a bid should be accepted. In the Consolidated Gold Fields case, we said that litigation taken without the consent of the shareholders may in some circumstances have the effect of frustrating a bid. In doing so, we were in no sense seeking to prevent a company from exercising its legal rights. We were simply indicating that where the effect of litigation might be to frustrate the bid, they should consult their shareholders first.

The other case I would like to mention by name is, of course, Guinness, which has been a concern of the Panel throughout the whole of my Chairmanship. The outcome is dealt with in more detail by the Director General. It was an anxious and difficult case, which I am glad has now been brought to a successful conclusion.

The Panel is, of course, founded on the commitment of practitioners. In particular, it is that commitment which gives the Panel its ability to call upon the expertise of senior City and industrial people, often at very short notice. In addition, that commitment is shown by the willingness of firms involved in takeovers to second people to the Panel Executive for two year periods, thus contributing substantially to its professionalism and awareness of developments in the market. I have depended greatly on the experience, support, and involvement of these individuals and firms.

This high level involvement must continue, since it is crucial to the Panel. I am personally very grateful for the warmth and support which colleagues have given me. I would like to make special mention of Mr. John Hull and Sir Philip Shelbourne, the Deputy Chairmen, whose experience and skills have been of great help to me.

The professionalism of the Executive is, to my mind, outstanding. It is, as always, difficult to pick out individuals but I would like to mention just a few.

John Walker-Haworth guided the Panel through a most difficult time under intense pressure. His skills, and strength of character, were of immense help to me in my first months. Antony Beevor has most skilfully maintained and enhanced the status and reputation of Director General during two years of much takeover activity, when a firm but enlightened approach was vital. It was a great pleasure that Peter Frazer deservedly received the OBE in recognition of his twenty years' service to the Panel. He, and Peter Lee, as Deputy Directors General, provide invaluable continuity and experience which guides those of us who stay a shorter time. The young staff of secondees, and our administrative and secretarial back-up, give devoted service. They work to demand - long hours and where necessary at weekends. This is no bureaucratic outfit. The City and industry get a service which responds to their needs for speedy but careful attention.

The Panel has over twenty-one years proved an effective regulatory body. There is, however, no cause for complacency. The world of takeovers is constantly changing and the Panel must constantly adapt and develop. It has to be recognised that the concept of non-statutory regulation is not one that is easily understood by everyone. In order to convince outsiders and to maintain confidence in the system, the Panel must, if anything, be even more effective and efficient than would be necessary were it a statutory body. This is an ongoing challenge.

Finally, I must touch briefly upon the proposed European Directive on Takeovers, which is also mentioned by the Director General in his report. The overriding concern in relation to that Directive must be to ensure that it is framed in such a way that it can be implemented in the United Kingdom through the existing non-legally binding system. The Panel has discussed this point extensively with the Commission and is encouraged by the impression we have gained that the Commission has no wish to undermine or require a radical change in that system, which it accepts is effective. I very much hope that further discussions with the Commission will result in agreement as to the means of implementation of the Directive but, until then, the matter is a cause for no little concern.

I hand over the Chairmanship of the Panel to David Calcutt QC, confident that the Panel will continue to be able to meet the challenges which lie ahead. I know that the Panel will benefit enormously from David's experience, expertise and wisdom. I am glad that the tradition of drawing the Chairman from outside the ranks of those who have been City practitioners is to continue. This, too, seems to me to be one of the Panel's strengths.

ALEXANDER OF WEEDON QC

27th September, 1989

REPORT BY THE DIRECTOR GENERAL

I begin by drawing attention to a number of developments which have taken place during the period since the publication of the last Annual Report.

Consortium Offers

Over the last year or so there has been a considerable amount of discussion about management buyouts, leveraged buyouts and other forms of consortium offers. Although the number of transactions which have actually taken place is not great, the Executive has received many enquiries as to the application of the Code to such transactions. They raise difficult problems. For example, one or more of the members of a proposed consortium may hold shares in the offeree company and, in connection with the proposed offer, effectively exchange those shares for shares in the vehicle established to make the offer. Such arrangements raise the question whether, to ensure similarity of treatment, all other shareholders should, in theory, be given the opportunity of exchanging their shares for shares in the offer vehicle, something which is clearly impractical in the circumstances of a buyout.

Other questions arise because consortium arrangements frequently involve one or more of the consortium members receiving benefits from the other consortium members such as rights to purchase parts of the offeree company's business. Such arrangements may be unobjectionable, but may also be a disguised way of paying the consortium member in question more for his offeree company shares than is proposed to be paid to other shareholders and the Panel is, as always, concerned to ensure that all shareholders are treated similarly.

Another point which can arise is that, when members of management propose a buyout, they place themselves in a position where their own interests may conflict with those of the company. It may be that the only practical protection available to the company's shareholders in these circumstances is already provided by Rule 3 of the Code, which aims to ensure the independence of the company's advisers (as instructed by those directors, if any, who are not part of the management buyout team).

The Panel has made some progress towards establishing its internal guidelines for answering these and other questions. The techniques will, however, develop with experience and it is consequently important that the Executive should be consulted in each case.

Guinness' offer for The Distillers Company

It was decided by my predecessor in the Spring of 1987 to investigate the facts that were then coming to light suggesting a breach of Rule 11 of the Code by Guinness. This arose out of the "Pipetec" purchase in the closing stages of Guinness' offer for Distillers in 1986. The matter was ultimately resolved when in July of this year details were announced of a remedy, involving the payment by Guinness of up to £85 million to certain former Distillers shareholders. The Panel has thus succeeded in arranging an appropriate remedy for those who were principally wronged, notwithstanding the significant obstacles and complications that it faced - not least the concurrent criminal proceedings involving some of those concerned with Guinness' offer.

The matter has been the subject of six sessions of the full Panel, two hearings before the Appeal Committee, hearings in the High Court and the Court of Appeal and an application to the House of Lords for leave to appeal to it. It is in many ways unsatisfactory that the matter took so long to resolve, but the right and, indeed, duty of the new management of Guinness to satisfy itself that it could fairly undertake the action ordered by the Panel has to be recognised. It is, however, an indication of the opportunities for delay when the legal system can be invoked and thus a further reminder, if that were needed, of the significance of the UK Courts' reluctance to adjudicate during the course of a takeover on Panel decisions, a matter to which the Chairman refers in his foreword.

The Panel process in the Guinness case was materially assisted by its ability to make use of the as yet unpublished DTI Inspectors' Report, extracts of which were, by permission of the Secretary of State, able to be shown in confidence to selected individuals in Guinness and its advisers.

Statutory Water Companies

During last year there was a high level of takeover activity in this sector, encouraged by the forthcoming privatisation of the water industry. This activity transformed what had previously been a very quiet sector of the market, with prices of listed stocks rising sharply.

The Introduction to the Code states that the Code applies, where appropriate, to statutory companies and, notwithstanding that statutory water companies do not have equity capital, the fact that investors were prepared to pay a premium to obtain votes bore heavily in the decision by the Executive that the Code should apply to these companies.

The idiosyncrasies of the rights attaching to the share capital of many of these companies brought a number of difficult and novel issues before the Executive. In particular, such issues as the requirement for comparability between offers for different classes of stock once again demonstrated the need for the Executive to be flexible and pragmatic in applying the Code to ensure that the underlying principles were met.

Meetings during offers

In the past, the restrictions in Rule 19 on the holding of meetings of selected shareholders effectively meant that no large meeting could be held because the Code required that all shareholders had to be invited. This meant that parties to offers frequently held a series of meetings involving only two people, one from the company and one analyst or investor. The Panel had long taken the view that it was difficult to apply the Rule 19 restrictions to 'one-to-one' meetings of this type, and the practice was unsatisfactory both for those involved and from the point of view of monitoring the release of information.

Accordingly, following representations from practitioners, a new Note 1 on Rule 19 was introduced in February 1989. This allows meetings of selected groups of shareholders to be held during an offer period, provided, of course, that no material new information is released or significant new opinions expressed, and provided the financial adviser or stockbroker to the party holding the meeting attends the meeting (even if it is a 'one-to-one' meeting) and confirms in writing to the Executive that no material new information has been released and no significant new opinions have been expressed.

The Executive will review how this new approach works in practice, particularly in the light of any comments received from practitioners or others directly affected.

European Community

There are two proposals being considered by the European Commission which have particular implications for the Panel and which the Executive has been discussing with representatives of the Department of Trade and Industry and the European Commission.

1. Proposal for a Thirteenth Council Directive on Company Law concerning takeover and other general bids, ("the takeover directive").

The takeover directive has now been adopted as a formal proposal by the European Commission and forwarded to the Council of Ministers and the European Parliament for consideration. The Panel assisted the UK delegation at the two meetings of the Council working party which were held in July.

The Panel is concerned that, while the primary objective of the directive, like that of the Code, is to ensure that shareholders are treated fairly during a takeover, nonetheless the directive may inadvertently create a system which increases the risk of litigation during a takeover and lacks the general flexibility that the Panel finds essential in its day to day operations.

The Panel believes that any body which regulates takeovers should be applying rules within the framework of a set of general principles; however, in the particular circumstances of a case, it must be possible for the regulatory body to grant dispensations from the rules. This right to derogate from the rules (which could not be written to cover all possibilities, present and future) is an essential requirement in an area where, as the Panel's 21 years of experience suggests, techniques are continually evolving. There is, at present, no general power of derogation in the draft takeover directive.

The other major concern of the Panel about the draft directive focuses on the method of implementation.

Directives are generally required to be implemented by means of legislation in such a way that the relevant rules have the force of law in the member country. This would, the Panel believes, inevitably lead to an increased risk of litigation, whether tactical or otherwise, during the course of takeovers. This would mean not only delay and expense, but also the loss of certainty that the Panel's rulings were final. In view of these concerns, the Panel has been discussing with the DTI and the European Commission how the directive might be implemented in a way which would retain the essential features of the current UK regulatory system. Clearly, such an approach would have to satisfy the requirements of European Law. While the Panel has been considering the takeover directive from the point of view of its own non-statutory status, it believes that the basic principles of flexibility and certainty are of importance to all takeover regulators.

These views correspond closely with the approach which the Government is taking in negotiations on the directive. In the meantime, the UK has formally placed a general reserve on the draft directive.

In addition to these fundamental points, the Panel has also raised a considerable number of concerns on the detailed contents of the directive.

2. Proposal for a Council Regulation on the control of concentrations between undertakings.

The Panel has been concerned to ensure that the authorities were aware of the existing offer timetable when formulating this proposal and of the need for an adequate filter mechanism. The roles of the Office of Fair Trading and the Monopolies and Mergers Commission have been cited as an example: the OFT acts as a filter, the result of which is that only a very small percentage of offers is referred to the MMC for further investigation. The OFT normally completes its work in time for the Secretary of State to announce his decision on whether an offer is to be referred by the first closing date of an offer (a maximum of seven weeks after the announcement of an offer). The latest formal proposal which the Panel has seen suggests that, while both points made by the Panel have been taken into account to some extent, there is not yet an adequate filter of the kind that the Panel considers appropriate, comparable to the OFT's screening of UK takeovers prior to investigation by the MMC. However, it is understood that further proposals are now under consideration which come significantly closer to meeting the Panel's objective.

Validation of acceptances and of purchases

Following the offer by Blue Circle Industries PLC for Birmid Qualcast PLC in which, inadvertently, certain shareholdings were counted twice, a Committee, under the chairmanship of Lord Rockley, was set up by the British Merchant Banking and Securities Houses Association to consider what action could be taken to prevent such a problem recurring. The Committee, which included representatives of all interested parties, produced a report which led to a number of amendments and additions of a technical nature to the Code.

While these changes may not have seemed of direct relevance to shareholders, it is clear that all parties connected with an offer, including offeree company shareholders, must be able to rely on the accuracy of a statement by the offeror that it has succeeded

in its offer. The Panel has therefore placed considerable responsibility on the receiving agents in an offer, who are required to satisfy themselves that the acceptances received or purchases made by an offeror are accompanied by documentation sufficient to classify them as up to registration standard. In this manner, it is considered that objective criteria have been laid down so that when the receiving agent produces a certificate such that the offeror can declare the offer unconditional as to acceptances, all parties can accept the validity of the figures.

Working Party on Takeover Rules and Practices

Companies Bill

The Panel recently had to consider suggestions that the Code does not do enough to restrict the acquisition of large share stakes by potential predators. This and other suggestions, some of which were made by the CBI, amongst others, were the subject of a report by a special working party, again chaired by Lord Rockley. This was considered by the Panel and a statement dealing with various issues which had become the subject of public discussion, together with the two changes to the Code which the Panel recommended, was released on 26th June, 1989.

The Panel views the proposals in the Companies Bill for the reduction of the present 5 per cent. threshold for disclosing a shareholding to 3 per cent. and a reduction of the period within which such disclosure has to be made from 5 business days to 2 business days as reducing some of the concerns expressed.

On its way through Parliament a number of amendments to the Bill were proposed which would have had the effect of making the Panel a statutory body. These amendments were resisted by the Government and were successfully rejected.

Chairmanship

It is naturally a matter of considerable sadness to the Executive that Robert Alexander's period of office as Chairman is about to end. He has achieved so much for the Panel that it is difficult to believe his term of office will have extended for only two and a half years. His contribution will last very much longer. The Chairmanship of National Westminster Bank will bring him further opportunities to display his enormous talents and we wish him well.

There are powerful advantages in having a senior member of the Bar as Chairman of the Panel. Such people have many calls on their time and the Panel is fortunate that David Calcutt QC, Master of Magdalene College, Cambridge and, among other things, President of the Appeal Tribunal of Lloyd's of London, should have accepted the Chairmanship of the Panel. He has already shown great interest in the Panel's work and we look forward to his official arrival in October.

27th September, 1989

REPORT ON THE YEAR ENDED 31st MARCH, 1989

STATISTICS

The Panel held 8 meetings to hear appeals by parties to takeover transactions against rulings by the Executive, 2 to consider disciplinary cases and 3 to consider cases referred by the Executive. None of the appeals were allowed. One case was heard by the Appeal Committee; it was not allowed. The Panel held a special meeting to consider various proposals for amendments to the Code.

There were 253 *(year ended 31st March, 1988–237)* published takeover or merger proposals of which 246 *(222)* reached the stage where formal documents were sent to shareholders. These proposals were in respect of 224 *(210)* target companies.

A further 24 *(22)* cases, which were still open at 31st March, 1989, are not included in these figures. The Executive was engaged in detailed consultations in another 195 *(186)* cases which either did not lead to published proposals or were transactions, subject to approval by shareholders, involving controlling blocks of shares.

Outcome of proposals	1988/9	*1987/88*
Successful proposals involving control (including Schemes of Arrangement) … … … …	184	*171*
Unsuccessful proposals involving control … …	40	*20*
Proposals withdrawn before issue of documents (including offers overtaken by higher offers) … …	7	*15*
Proposals involving minorities … … …	22	*31*
	253	237

STAFF

The following changes in the Executive have taken place since the publication of the last Annual Report.

Mr. J. G. Doctor, formerly of Kitcat & Aitken, has been appointed Assistant Director General. Mr. N. P. Hinton, previously Joint Secretary, has also been appointed Assistant Director General. Mr. A. S. Clark of Ashurst Morris Crisp has been appointed Joint Secretary. Miss. S. M. Govier, previously an Assistant Secretary, has also been appointed Joint Secretary.

Mr. R. J. Hilton, Mr. B. C. K. Timbrell, Mr. S. A. Atkinson, Mr. W. J. Morgan and Mr. A. M. Keir have left the Executive. Mr. C. J. Bailey of the Department of Trade and Industry, Miss C. E. Hambro of Hambros Bank Limited, Mr. A. J. Strachan of the Bank of England and Mr. T. P. Kennedy of the Royal Bank of Scotland have joined the Executive.

Finance

During the period covered by this Report the Panel was financed by charges in relation to offer documents, a fee agreed with The Stock Exchange and Panel members' contributions. Details of the document charges are set out in the Code.

Expenditure for the year to 31st March, 1989 was as follows:–

	(£000)	
	1989	*1988*
Personnel costs	1,543	*1,381*
Accommodation costs	658	*276*
Other	974	*791*
	3,175	*2,448*

During the year, the staff was further increased and the premises considerably altered to accommodate this.

(Further copies of the Report may be obtained from the Secretary, Panel on Takeovers and Mergers, P.O. Box No 226, The Stock Exchange Building, London, ***EC2P 2JX****.)*