



EUROPEAN COMPANY LAW

Draft Directive on
Cross-Border Mergers

A CONSULTATIVE DOCUMENT

JUNE 2004



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EUROPEAN COMPANY LAW - DRAFT DIRECTIVE ON CROSS-BORDER MERGERS

June 2004

The Department of Trade and Industry invites comments, by **20 September 2004** on the issues set out in this paper.

You are invited to send comments, together with any supporting evidence on any part of this consultation, preferably by email, to:

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Questions relating to company law should be directed to Jessica White. Questions relating to employee participation should be directed to:

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Open Government: Under the Code of Practice on Access to Government Information comments may be made publicly available unless consultees state otherwise. Consultees should therefore indicate whether their responses should be treated as confidential. A summary of responses will be published on the website.

We will handle any personal data you provide appropriately in accordance with the Data Protection Act 1998.

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1. INTRODUCTION

- 1.1 This consultation document seeks your views on the proposal for a Company Law Directive on Cross-Border Mergers published by the European Commission on 18 November 2003. The full text of the Directive is set out at Annex B¹.
- 1.2 The proposed Directive seeks to establish common rules across the EU governing cross-border mergers. The Commission intends that the proposal should extend to companies with share capital from different EU Member States. The proposed Directive would allow companies across the EU to merge cross-border based on the approach taken in the Third Company Law Directive, which applies to domestic company mergers of public limited companies, and the cross-border provisions in the European Company Statute.
- 1.3 Currently, Part XIII of the Companies Act 1985 governs domestic mergers, dealing with Arrangements and Reconstructions (under sections 425 - 430). These provisions apply to both public and private companies incorporated under the Companies Act 1985. There are presently no specific procedures under GB law for cross-border mergers, although a number of devices have been used by business to achieve cross-border restructuring involving GB incorporated companies, such as takeovers and dual listing arrangements.
- 1.4 Government supports the facilitation of corporate restructuring activities across the European Union to promote the Single Market. An effective framework of European company law is essential for the internal market and building an integrated European capital market. Government agrees with the Commission that work should be undertaken on this Directive to facilitate cross-border mergers and considers the right solution will be a Directive that is clear on scope, increases legal certainty, is effective and provides adequate safeguards for those who deal with the companies involved. It is critical that the final provisions of the Directive offer a practical solution for corporate restructuring in cross-border merger activity.

Your opportunity to comment:

- 1.5 We have tried to present the issues as clearly as possible in non-technical terms. A glossary of technical terms is included at Annex C. Please contribute comments and evidence, especially on costs and benefits of the present proposal to Jessica White at the Department of Trade and Industry by **20 September 2004**.

¹ The full text is also available on http://europa.eu.int/eur-lex/pri/en/lip/latest/doc/2003/com2003_0703en01.doc

2. BACKGROUND

2.1 The objective of this Directive is to create a legal framework for companies to merge between Member States where none presently exists. A previous version of this proposal was published in 1984. However, it was withdrawn in 2001 when agreement could not be reached on provisions for employee participation rights. The new proposal is based on the Third Company Law Directive², for domestic company mergers, incorporated into GB law in the Companies Act 1985. Corporate restructuring through use of the merger procedure under the Directive will be optional. The opportunity to bring proposals forward arises as a consequence of recent developments in European company law:-

- A Cross-Border Mergers Directive is a commitment under the Lisbon Financial Services Action Plan to create an integrated European Single Market by 2005³;
- High Level Group of Company Law Experts appointed by the Commission in September 2001 who, amongst other issues, examined the possibility of facilitating cross-border company mergers; and
- A Cross-Border Mergers Directive is part of the EU Action Plan on Company Law and Corporate Governance published by the Commission in May 2003⁴.

3. THE PROPOSALS

3.1 Article 1 - Scope of the Directive:

A key objective is to aid cross-border restructuring by companies that do not necessarily want to form a European Company under the European Company Statute (ECS). The European Company Statute Regulation⁵ (which takes effect in October 2004 and allows "European companies" (SEs) to be formed by cross-border merger) is supplemented by a Directive regarding employee involvement in the SE.

2 Third Council Directive (EEC) No 78/855 of 9 October 1978

3 Communication of the Commission, COM (1999) 232 of 11 May 1999

4 Communication of the Commission, COM (2003) 284 of 21 May 2003

5 Council Regulation (EC) No 2157/2001 of 8 October 2001 and Council Directive (EC) No 2001/86 of 8 October 2001

- 3.2 The Directive will apply to any 'company with share capital', which is defined at Article 1 and will have the effect of including both private companies and public companies. This is broader than the original 1984 proposal and goes further than the Third Company Law Directive on domestic company mergers, which only applies to public limited companies.
- 3.3 To clarify which companies will be caught under Article 1, the text could be amended to give a more precise definition of 'company with share capital' or by listing the types of companies that the Directive would apply to. However, a list may be inflexible and would be in need of updating to reflect new forms of companies created within the EU.

Q1 Are you happy with the scope of the Directive?

Q2 Do you think that the current definition of 'company with share capital' is sufficiently clear or, if not, how might this be improved?

3.4 Article 1 - Types of transaction:

The Directive aims to capture transactions where shareholders exchange shares in the transferring companies substantially in return for shares in the merged companies. Any cash consideration for the transaction is limited to 'a cash payment not exceeding 10% of the nominal value, or in absence of a nominal value, of the accounting par value of those securities or shares'. However, the nominal (or accounting par value) value may not be an accurate reflection of the true economic value of the companies involved. This is more likely to be indicated by the market price of the shares, and a limit of 10% may be seen as unnecessarily restrictive of the types of transactions that should properly be caught by the proposal. In order to amend this, a more appropriate solution may be to prescribe the types of transaction by reference to some fraction (for example, 10%) of the net asset value of the transaction.

Q3 Should there be a limit on the size of the cash allowance in merger transactions under the proposal?

Q4 If there is a limit on the size of cash payment, how should this be calculated and at what level should it be set (i.e. by reference to the nominal/accounting par value, as in the Commission proposal, or other criteria, such as the total value of the assets involved in the merger transaction)?

3.5 Tax implications

Tax issues related to cross-border mergers are dealt with under the tax mergers Directive (90/434/EEC). In October 2003, the Commission issued a formal proposal to amend this Directive. This proposal is currently the subject of discussions between Member States in a Council Working Group. The Inland Revenue is already considering the implications for tax legislation of the European Company Statute provisions relating to cross-border mergers to form SEs. The Revenue will consult separately on any tax changes required by the Cross-Border Mergers Directive.

4. FORMALITIES OF THE MERGER

4.1 The procedure for a cross-border merger is based on the Third Company Law Directive for domestic mergers and is dealt with in:

- Article 2 - Each company will remain subject to its national law on domestic mergers (except for adjustments to take into account the cross-border nature of the transaction). In GB, Part XIII of the Companies Act 1985 governs domestic mergers and applies to both public and private companies. It deals with matters such as meetings of shareholders to consider the merger proposal, creditor protection and court approval;
- Articles 3, 4 and 5 - Draft terms of merger must be drawn up by administrative / management bodies of each of the companies involved and reported upon by experts. These experts may require any information on the company that they need in the exercise of their duties. There is also a requirement to publish certain details about the merger at least one month prior to its consideration by a general meeting of the company. Detailed provisions related to the drawing up and publication of draft merger terms and reports by experts are contained in Schedule 15B to the Companies Act 1985 (which applies to domestic mergers of public limited companies);
- Article 6 - A general meeting of each of the merging companies is required to approve the draft terms of the merger;
- Articles 7 and 8 - Scrutiny of the legality of the cross-border elements of the merger is based on provisions contained in the European Company Statute Regulation. This includes a requirement for the relevant Member States to designate a competent authority to scrutinise the legality of the merger as regards any national provisions. For domestic mergers in GB, it is the court which considers the legality of the proposed merger;

- Article 9 - The date from which the merger takes effect shall be decided by the law of the relevant Member State in which the acquiring or newly formed company is situated; and
- Article 12 - After the date the merger takes effect, the merger cannot be declared null and void. These articles combined with the provisions under Article 9 aim to ensure legal certainty.

Q5 Are you satisfied that the proposal's approach, relying on Member States' domestic merger laws, offers adequate protection to creditors and members, in the dissolving company(ies)? If not, what more could be included?

Q6 Do you think the Directive is clear enough that national law will govern the merger procedure and the newly formed company?

5. ARTICLE 14 - EMPLOYEE PARTICIPATION:

5.1 On employee involvement, the Commission have not sought to include employee information and consultation provisions, which they accept are adequately addressed at national and transnational level by existing employment legislation (particularly the Information and Consultation Directive and the European Works Council Directive).

5.2 There are at present no EC level rights or protections in relation to employee participation, other than those in relation to the voluntary ECS, adopted in October 2001 and entering into force on 8 October 2004. A consultation document, *"Implementation of the European Company Statute: The European Public Limited-Liability Company Regulations 2004"*, was published in October 2003⁶, the responses to which are now being considered by Government. This consultation document contains a copy of the ECS Directive (which deals with employee involvement aspects of the ECS) and Government's proposals for its domestic implementation.

5.3 Employee participation is essentially a system that exists in some Member States (such as Germany, Austria, Netherlands and Sweden) and gives employees the statutory right to involvement at Board level (a more complete definition of participation is included at Annex C). The UK does not have such a mandatory system.

6 The document may be found on the DTI website: <http://www.dti.gov.uk/cld/condocs.htm>

Proposed Article 14 provisions

- 5.4 The Directive does not impose any new participation requirements where employee participation rights do not exist in any of the merging companies.
- 5.5 The Commission state that a company created by cross-border merger operations under this Directive will be governed by existing national rules on participation in the Member State in which its registered office is situated. These companies will remain subject to the compulsory participation rules applicable in that Member State. Therefore, where a merged company registers in a Member State that imposes compulsory participation rules, those rules would apply throughout the new company. For example, where a UK company merges with a German company and incorporates in Germany, the German rules on employee participation would apply to the entire company. Where both merging companies have existing employee participation arrangements (for example, a German and Dutch company), the merged company would apply the participation rules of whichever Member State it is finally registered in, without the need for a negotiation process.
- 5.6 Where participation arrangements exist in one or more of the merging companies but the law of the Member State applicable to the company created by the merger does not impose compulsory employee participation, Article 14 requires Member States to regulate the process of drawing up participation rights in accordance with the principles and provisions contained in the ECS Directive. These would require a process of negotiating with employee representatives for up to 12 months to agree the employee participation arrangements (including the board structure) that will exist in the merged company. Where no agreement is reached, a set of standard rules on participation would apply. The merger could not be completed until this process had been carried out.
- 5.7 The negotiation process would require the setting up of a Special Negotiating Body (SNB), representing all the employees of all the merging companies. SNB representatives must be elected or appointed in accordance with rules drawn up by individual Member States. The competent organs of the merging companies are required to meet all costs of the negotiation process (including the cost of experts assisting the SNB). All decisions of the SNB must be taken by an absolute majority of the SNB members, representing an absolute majority of the employees. In all cases, the highest "level" of employee participation rights must be maintained and extended across the merged company as had previously existed in any of the merging companies, unless the SNB decides otherwise. However, where at least 25% of the overall numbers of employees have participation rights, a special two-

thirds majority decision of the SNB is required for any reduction in the level of participation rights. The standard rules that apply where there is no agreement would give the employees of the merged company, its subsidiaries and establishments and/or their representative body the right to elect, appoint, recommend or oppose the appointment of a number of members of the administrative or supervisory body of the merged company equal to the highest proportion in force in the merging companies. The standard rules impose no requirements in relation to the board structure of the merged company. However, where more than one form of participation existed between the merging companies, it would be for the SNB to decide which form should exist within the merged company.

- 5.8 Like the ECS Directive, Article 14 also gives Member States the option of not applying the standard rules relating to participation. However, use of this option would effectively prevent any merged company from registering in that country unless there are no existing participation rights in any of the merging companies or a voluntary agreement has been reached that provides for participation if it previously existed in the participating companies.

Issues to consider

- 5.9 Fairness and Proportionality: The process of negotiating participation arrangements would apply only where a merged company, which previously had some participation, wishes to register in a Member State, like the UK, that does not impose compulsory participation rules. The effects would be that the highest level of participation that existed in the merging company would, in most cases, be extended to all employees in the new company.
- 5.10 Choice and flexibility for companies: The current provisions in Article 14 for harmonising different employee participation arrangements within the merging companies may artificially distort merger decisions if, when seeking out suitable merger opportunities, companies look for partners with comparable participation regimes (to avoid the need for negotiations), or no participation rights at all.
- 5.11 Practicalities: These provisions are complex and the duration of the negotiation process that is required before a merger can be completed could deter companies from opting for a cross-border merger.

Q7 Can you suggest any improvements to the provisions in Article 14 and, in particular, any suggestions that might address the issues highlighted above?

Q8 Do you have any other comments on the provisions in Article 14?

6. COSTS, SAVINGS AND BENEFITS

6.1 A draft regulatory impact assessment (RIA) is attached at Annex D.

Q9 We would welcome comments and evidence on the RIA, especially on the savings and benefits (or any costs) of the proposed Directive. Comments are also invited on any unintended consequences or other implications.

What happens next?

Discussions on the proposed Cross-Border Mergers Directive have already begun in Council Working Groups. In view of the proposal's status as remaining uncompleted items under the Financial Services Action Plan and as a priority measure under the EU Action Plan on Company Law and Corporate Governance, it is likely that there will be the requisite political will to secure early agreement to this proposal.

Note to Consultees - although we are unable to control the EU negotiation timetable, early comments (even if not fully formulated) would be gratefully received.

Help with queries

7. If you have comments or complaints about the way this consultation has been conducted, these should be sent to:

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Department of Trade and Industry
1 Victoria Street
London SW1H 0ET
louisa.renwick@dti.gsi.gov.uk

Annex A

Summary of Questions

- Q1** Are you happy with the scope of the Directive?
- Q2** Do you think that the current definition of 'company with share capital' is sufficiently clear or, if not, how might this be improved?
- Q3** Should there be a limit on the size of the cash allowance in merger transactions under the proposal?
- Q4** If there is to be a limit on the size of cash payment, how should this be calculated and at what level should it be set (i.e. by reference to the nominal/accounting par value, as in the Commission proposal, or other criteria, such as the total value of the assets involved in the merger transaction)?
- Q5** Are you satisfied that the proposal's approach, relying on Member States' domestic merger laws, offers adequate protection to creditors and members, in the dissolving company(ies)? If not, what more could be included?
- Q6** Do you think the Directive is clear enough that national law will govern the merger procedure and the newly formed company?
- Q7** Can you suggest any improvements to the provisions in Article 14 and, in particular, any suggestions that might address the issues highlighted in this consultation?
- Q8** Do you have any other comments on the provisions in Article 14?
- Q9** We would welcome comments and evidence on the RIA, especially on the savings and benefits (or any costs) of the proposed Directive. Comments are also welcomed on any unintended consequences or other implications.

Annex B

COMMISSION OF THE EUROPEAN COMMUNITIES



Brussels, 18.11.2003
COM(2003) 703 final
2003/0277 (COD)

Proposal for a

DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL

on cross-border mergers of companies with share capital

(presented by the Commission)

EXPLANATORY MEMORANDUM

1. PURPOSE OF AND GROUNDS FOR THE PROPOSAL

The purpose of the Directive, which is to be viewed against the background of the Financial Services Action Plan and the Communication from the Commission to the Council and the European Parliament of 21 May 2003 entitled *Modernising Company Law and Enhancing Corporate Governance in the European Union - A Plan to Move Forward*, is to fill a significant gap in company law left by the need to facilitate cross-border mergers of commercial companies without the national laws governing them - as a rule the laws of the countries where their head offices are situated - forming an obstacle.

At present, as Community law now stands, such mergers are possible only if the companies wishing to merge are established in certain Member States. In other Member States, the differences between the national laws applicable to each of the companies which intend to merge are such that the companies have to resort to complex and costly legal arrangements. These arrangements often complicate the operation and are not always implemented with all the requisite transparency and legal certainty. They result, moreover, as a rule in the acquired companies being wound up - a very expensive operation.

There is an increasing need today in the Community of Fifteen for cooperation between companies from different Member States, as there will be tomorrow in the future enlarged Union, not forgetting the EFTA countries.

For a number of years now, Community companies have been calling for the adoption of a Community legal instrument that meets their needs for cooperation and consolidation between companies from different Member States and that enables them to carry out cross-border mergers.

More than ever, all companies, whether they be public limited liability companies or any other type of company with share capital, must have at their disposal a suitable legal instrument enabling them to carry out cross-border mergers under the most favourable conditions. The costs of such an operation must therefore be reduced, while guaranteeing the requisite legal certainty and enabling as many companies as possible to benefit. The scope of the Directive will therefore be drawn in such a way as to cover above all small and medium-sized enterprises, which stand to benefit because of their smaller size and lower capitalisation compared with large enterprises and for which, for the same reasons, the European company Statute does not provide a satisfactory solution.

2. HISTORICAL CONTEXT

On 14 December 1984 the Commission adopted a proposal for a tenth Council Directive on cross-border mergers of companies.⁷ Several committees of the European Parliament examined the proposal, including the Committee on Legal Affairs, which adopted its report on 21 October 1987.⁸ However, Parliament did not deliver its opinion owing to the difficulties raised by the problem of employee participation in companies' decision-making bodies. This situation of deadlock, which was linked to the fate of the proposal for a European company Statute, lasted more than 15 years. In 2001, against the backdrop of a wholesale withdrawal of proposals which had been pending for several years or which had become devoid of purpose, the Commission withdrew this first proposal for a tenth Directive with a view to presenting a fresh proposal based on the latest developments in Community law. A resolution of the European company (SE) question having been reached on 8 October 2001, the work on preparing a new proposal for a Directive on cross-border company mergers accordingly resumed. In the light of this state of affairs and of the fact that the parties have had an opportunity to comment on the broad lines of the proposal, both as part of the consultations carried out by the High-Level Group of Company Law Experts and as part of those on the above-mentioned Commission communication of 21 May 2003, further consultations and impact assessment on the present proposal, the speedy adoption of which is wished for by the interests concerned, have not been considered necessary.

3. FEATURES OF THE PROPOSAL

The present proposal differs from the original proposal of 1984 mainly in scope and in the way it takes account, with regard to the participation of employees in the decision-making bodies of the acquiring company or of the new company created by the cross-border merger, of the principles and solutions incorporated in Council Regulation (EC) No 2157/2001 of 8 October 2001 on the Statute for a European company (SE)⁹ and in Council Directive 2001/86/EC of 8 October 2001 supplementing the Statute for a European company with regard to the involvement of employees.¹⁰

3.1. Scope

The original proposal covered only public limited liability companies. The present

7 OJ C 23 25.1.1985, p. 11.

8 PE/113303/JUR/FIN, A2/1987/186.

9 OJ L 294, 10.11.2001, p. 1.

10 OJ L 294, 10.11.2001, p. 22.

proposal extends that scope to include all companies with share capital which, in the unanimous view of the Member States, may be typified as companies having legal personality and separate assets which alone serve to cover the company's debts. It is aimed primarily at companies which are not interested in forming an SE, i.e. for the most part small and medium-sized enterprises.

3.2. Principles governing the cross-border merger procedure

The basic principle underlying the cross-border merger procedure is that - save as otherwise provided by the Directive for reasons to do with the cross-border nature of the merger - the procedure is governed in each Member State by the principles and rules applicable to mergers between companies governed exclusively by the law of that State (domestic mergers).

The aim is to approximate the cross-border merger procedure with the domestic merger procedures with which operators are already familiar through use. In order to take account of the cross-border aspects, the principle of the application of national law is incorporated - but no more than is strictly necessary - via provisions based on the relevant principles and rules already laid down for the formation of an SE.

Protection under national law is also afforded to the interests of creditors, debenture holders, the holders of securities other than shares, minority shareholders and employees, as regards rights other than those related to participation in the company, vis-à-vis each of the merging companies. Reference may be made here to Council Directive 2001/23/EC of 12 March 2001 relating to the safeguarding of employees' rights in the event of transfers of undertakings,¹¹ Directive 2002/14/EC of the European Parliament and of the Council of 11 March 2002 establishing a general framework for informing and consulting employees in the European Community,¹² and Council Directive 94/45/EC of 22 September 1994¹³ and Council Directive 97/74/EC¹⁴ of 15 December 1997, both of which concern the establishment of a European works council or a procedure in Community-scale undertakings and Community-scale groups of undertakings for the purposes of informing and consulting employees. These Directives also apply to companies created by a cross-border merger.

The Directive, as is the case for comparable previous legal acts¹⁵, is without

11 OJ L 82, 22.3.2001, p. 16.

12 OJ L 80, 23.3.2002, p. 29.

13 OJ L 254, 30.9.1994, p. 64.

14 OJ L 10, 16.1.1998, p. 22.

15 Third Council Directive concerning mergers of public limited liability companies (78/855/EEC) (OJ L 295, 20.10.1978, p.36).

prejudice to the application of the legislation on the control of concentrations between undertakings, both at the Community level¹⁶ and at the level of Member States.

3.3. Employee participation and company law coordination

Employee participation in a company created by cross-border merger, which was the reason for the deadlock over the original proposal of 1984, is coordinated by the present proposal for a Directive with a view to ensuring freedom of establishment.

The overriding fear concerning cross-border mergers was that the process might be hijacked by companies which, faced with having to live with employee participation, might try to circumvent it by means of such a merger.

Regulation (EC) No 2157/2001 and Directive 2001/86/EC have come up with a solution which can be used, *mutatis mutandis*, also with a view to coordinating company law under Article 44(2)(g) of the EC Treaty, as is the purpose of this Directive.

The context in which the Regulation and the Directive on the SE operate is different, however, from that surrounding the application of this Directive. By virtue of its Community nature, the SE is not subject to any existing national rules on compulsory participation in the Member State in which its registered office is situated. By contrast, companies created by the cross-border merger operations covered by the present Directive will be companies governed by the law of a Member State. Such companies will accordingly remain subject to the compulsory participation rules applicable in that Member State. It may well be, however, that, following a cross-border merger, the registered office of the company created by the merger is situated in a Member State which does not have this type of rule, whereas one or more of the companies taking part in the merger were operating under a participation system before the merger. To deal with this eventuality, provision is made for extending to companies covered by the present Directive the same protection of rights acquired with respect to participation as is granted under the system set up by the SE Regulation and Directive. The protection of acquired rights of participation is entirely justified in this case. In cases where the national law of the Member State by whose law the company created by the merger is governed does have rules on compulsory employee participation, such specific protection is unnecessary as the company in question will be subject to those rules.

¹⁶ Council Regulation (EEC) No 4064/89 on the control of concentrations between undertakings, OJ L 395, 30.12.1989, p.1; corrected version OJ L 257, 21.9.1990, p. 13, Regulation as last amended by Regulation (EC) No 1310/97, OJ L 180, 9.7.1997, p.1; corrigendum in OJ L 40, 13.2.1998, p. 17.

4. COMMENTS ON THE ARTICLES

Article 1 contains definitions which serve to delimit the scope of the Directive. The definitions of merger by acquisition and merger by the formation of a new company are taken from Directive 90/434/EEC, which also covers mergers between companies from different Member States and forms of company other than public limited liability companies. These definitions are in keeping with those in Directive 78/855/EEC concerning domestic mergers of public limited liability companies.¹⁷ The scope includes all Community companies with share capital which, in the unanimous view of the Member States, may be typified as companies having legal personality and separate assets which alone serve to cover the company's debts. It is wider than that of Directive 78/855/EEC in that it is not limited to public limited liability companies but covers all companies with share capital.

Article 2 is designed to identify the law applicable in the event of a cross-border merger to each of the merging companies. Save as otherwise provided by the present Directive for reasons to do with the cross-border nature of the operation, each company remains subject to its national law on domestic mergers.

As to the protection of employees, the cross-border merger remains subject, with regard to rights other than those of participation in the acquiring company or in the new company created by the cross-border merger, to the relevant provisions applicable in the Member States, as harmonised *inter alia* by Council Directive 2001/23/EC of 12 March 2001 relating to the safeguarding of employees' rights in the event of transfers of undertakings, Directive 2002/14/EC of the European Parliament and of the Council of 11 March 2002 establishing a general framework for informing and consulting employees in the European Community and Directives 94/45/EC and 97/74/EC concerning the establishment of a European works council and the informing and consulting of employees. By virtue of these provisions, the change of employer resulting from the merger operation must have no effect on the contract of employment or employment relationship in force at the time of the merger, which is automatically transferred to the new owner. Likewise protected after the merger are all acquired rights of employees agreed under a collective agreement, and their rights to old-age, invalidity or survivor's benefits under statutory social security schemes.

Article 3 lists the points that have to be included in the draft terms of cross-border merger. It includes the items already harmonised by Directive 78/855/EEC for domestic mergers of public limited liability companies, to which have been added, as in the case of the SE, a number of further items dictated by the cross-border nature of the operation, such as the name and registered office proposed for the

17 OJ L 295, 20.10.1978, p. 36.

new company. The place where the registered office is situated determines which law will be applicable to the new company - an important piece of information as far as all interested parties, including creditors, are concerned. The draft terms must also contain information on the arrangements for employee involvement in decisions taken by the company created by the cross-border merger.

Article 4 deals with publication of the draft terms of cross-border merger and the information that must be furnished.

Article 5 provides for the possibility, as already laid down by Directive 78/855/EEC for domestic mergers of public limited liability companies and by Regulation (EC) No 2157/2001 for the European company, of providing for a single expert report on behalf of all shareholders.

Article 6 lays down the requirement of approval of the draft terms of cross-border merger by the general meeting. A similar requirement exists in the case of domestic mergers of public limited liability companies and in that of the formation of an SE by merger.

Articles 7 and 8 govern scrutiny of the legality of cross-border mergers. They are based on the corresponding principles and techniques provided for in Regulation (EC) No 2157/2001 for the SE.

Article 9 concerns the date on which the cross-border merger takes effect. The relevant date is to be that provided for by the law of the Member State by which the acquiring company is governed in the case of cross-border merger by acquisition or by which the new company is governed in the case of cross-border merger by the formation of a new company. The date must be after all the checks on all the companies taking part in the operation have been carried out.

Article 10 deals with the disclosure that must be effected upon completion of a cross-border merger. It is based on the corresponding provisions of Article 3 of Directive 68/151/EEC on the safeguards required to protect the interests of members and others,¹⁸ this being the article that governs the publicising of all essential documents relating to companies with share capital.

Article 11 is based on Articles 19 and 23 of Directive 78/855/EEC, which already coordinate the effects of a domestic merger for public limited liability companies.

Article 12 is based on Article 29 of Regulation (EC) No 2157/2001, according to which, after the date on which a cross-border merger takes effect, it is no longer

18 OJ L 65, 14.3.1968, p. 8.

possible to declare the merger null and void, the aim being to ensure absolute certainty for all third parties affected by the merger in the various Member States concerned. It would be highly dangerous for third parties subject to the laws of different Member States to be faced with the nullity of an operation after all the checks in each Member State had been carried out conclusively.

Article 13 seeks to simplify the cross-border merger procedure in the case of a merger between two companies where the acquiring company already holds all or most of the shares or other securities of the company being acquired that confer the right to vote at the latter's general meetings. In such cases, a number of steps can in fact be dispensed with.

Article 14 deals with the participation of employees in the company created by a cross-border merger where the protection of acquired rights of participation is put at risk by the merger. Article 14 is relevant only in a situation where one of the merging companies has a participation regime, be it compulsory or voluntary and the law of the Member State where the company created by merger is to be incorporated does not impose compulsory employee participation. In all other cases, the national law applicable to the company created by merger determines the rules on employees' involvement. Article 14 reflects the balance already found in the context of the European Company Statute, in particular the negotiation procedure which should enable the interested parties to negotiate an appropriate regime to be applied for employee participation. For this purpose, article 14 incorporates by reference the provisions of Directive 2001/86/EC and Part 3 of the Annex which are specifically relevant to mergers. Accordingly, it is only if the merging companies fail to reach a negotiated solution, that the participation system which best protects the acquired rights of the workers and which already exists in one of the merging companies is extended to the company created by merger.

Articles 15 and 16 contain the usual final provisions concerning implementation, entry into force and the addressees of the Directive.

2003/0277 (COD)

Proposal for a

DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL

on cross-border mergers of companies with share capital

(Text with EEA relevance)

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION,
Having regard to the Treaty establishing the European Community, and in particular Article 44(1) thereof,
Having regard to the proposal from the Commission,¹⁹
Having regard to the opinion of the European Economic and Social Committee,²⁰
Having regard to the opinion of the Committee of the Regions,²¹
Acting in accordance with the procedure laid down in Article 251 of the Treaty,
Whereas:

- (1) The need for cooperation and consolidation between companies from different Member States and the difficulties encountered, at the legislative and administrative levels, by cross-border mergers of companies in the Community make it necessary, with a view to the completion and functioning of the single market, to lay down Community provisions to facilitate the carrying-out of cross-border mergers between various types of company with share capital governed by the laws of different Member States.
- (2) The above-mentioned objectives cannot be sufficiently attained by the Member States in so far they involve laying down rules with common features applicable at transnational level; owing to the scale and impact of the proposed action, they can therefore best be achieved at Community level, it being possible for the Community to take measures in accordance with the principle of subsidiarity laid down in Article 5 of the Treaty. In accordance with the principle of proportionality as set forth in that article, this Directive does not go beyond what is necessary to achieve those objectives.
- (3) In order to facilitate cross-border merger operations, it should be laid down that, unless this Directive provides otherwise, each company taking part in a

19 OJ C [...], [...], p. [...].

20 OJ C [...], [...], p. [...].

21 OJ C [...], [...], p. [...].

merger, and each third party concerned, remains subject to the provisions of national law by which the company is governed, being those provisions which are applicable in the event of a merger with other companies governed by the same law.

- (4) The common draft terms of cross-border merger must be drawn up in the same terms for each of the companies concerned in the various Member States. The minimum content of such common draft terms should therefore be specified, while leaving the companies free to agree on other items.
- (5) In order to protect the interests of members and others, both the draft terms of merger and the completion of the merger must be publicised for each merging company via an entry in the appropriate public register.
- (6) The laws of all the Member States provide for the drawing-up of a report on the draft terms of merger by one or more experts on behalf of each of the companies that are merging at national level. In order to limit experts' costs connected with cross-border mergers, provision should be made for the possibility of drawing up a single report intended for all members of companies taking part in a cross-border merger operation. The common draft terms of cross-border merger must be approved by the general meeting of each of these companies.
- (7) In order to facilitate cross-border merger operations, it should be provided that monitoring of the completion and legality of the decision-making process in each merging company should be carried out by the national authority having jurisdiction over each of those companies, whereas monitoring of the completion and legality of the merger should be carried out by the national authority having jurisdiction over the company created by the merger. The latter authority may be a court, a notary or any other competent authority appointed by the Member State concerned. The national law determining the date on which the merger takes effect - this being the law to which the company created by the merger is subject - should also be specified.
- (8) In order to protect the interests of members and others, the legal effects of the cross-border merger - distinguishing according to whether the company created by the merger is an acquiring company or a new company - should be specified. In the interests of legal certainty, it should no longer be possible, after the date on which a cross-border merger takes effect, to declare the merger null and void.
- (9) This Directive is without prejudice to the application of the legislation on the

control of concentrations between undertakings, both at the Community level²² and at the level of Member States.

- (10) Employees' rights other than rights of participation should remain subject to the national provisions referred to in Council Directive 98/59/EC of 20 July 1998 on the approximation of the laws of the Member States relating to collective redundancies,²³ Council Directive 2001/23/EC of 12 March 2001 on the safeguarding of employees' rights in the event of transfers of undertakings,²⁴ Directive 2002/14/EC of the European Parliament and of the Council of 11 March 2002 establishing a general framework for informing and consulting employees in the European Community²⁵ and Council Directive 94/45/EC of 22 September 1994 on the establishment of a European Works Council or a procedure in Community-scale undertakings and Community-scale groups of undertakings for the purposes of informing and consulting employees.²⁶
- (11) If at least one of the companies taking part in the cross-border merger is operating under a participation system and if the national law of the Member State in which the registered office of the company created by the merger is situated does not impose compulsory employee participation on that company, the participation of employees in the company created by the cross-border merger and their involvement in the definition of such rights must be regulated. To that end, the principles and procedures provided for in Council Regulation (EC) No 2157/2001 of 8 October 2001 on the Statute for a European company²⁷ and in Council Directive 2001/86/EC of 8 October 2001 supplementing the Statute for a European company²⁸ should be taken as a basis,

HAVE ADOPTED THIS DIRECTIVE:

Article 1

For the purposes of this Directive:

22 Council Regulation (EEC) No 4064/89 on the control of concentrations between undertakings, OJ L 395, 30.12.1989, p. 1; corrected version OJ L 257, 21.9.1990, p. 13, Regulation as last amended by Regulation (EC) No 1310/97, OJ L 180, 9.7.1997, p.1; corrigendum in OJ L 40, 13.2.1998, p. 17.

23 OJ L 225, 12.8.1998, p. 16.

24 OJ L 61, 5.3.1977, p. 26.

25 OJ L 80, 23.3.2002, p. 29.

26 OJ L 254, 30.9.1994, p. 64; Directive amended by Directive 97/74/EC (OJ L 10, 16.1.1998, p. 22).

27 OJ L 294, 10.11.2001, p. 1.

28 OJ L 294, 10.11.2001, p. 22.

- *“merger”* means an operation whereby:
 - (a) one or more companies, on being dissolved without going into liquidation, transfer all their assets and liabilities to another existing company - the acquiring company - in exchange for the issue to their shareholders of securities or shares representing the capital of that other company and, if applicable, a cash payment not exceeding 10% of the nominal value, or, in the absence of a nominal value, of the accounting par value of those securities or shares; or
 - (b) two or more companies, on being dissolved without going into liquidation, transfer all their assets and liabilities to a company that they form - the new company - in exchange for the issue to their shareholders of securities or shares representing the capital of that new company and, if applicable, a cash payment not exceeding 10% of the nominal value, or in the absence of a nominal value, of the accounting par value of those securities or shares; or
 - (c) a company, on being dissolved without going into liquidation, transfers all its assets and liabilities to the company holding all the securities or shares representing its capital;

- *“cross-border merger”* means a merger within the meaning of the first indent which involves companies with share capital formed in accordance with the law of a Member State and having their registered office, central administration or principal place of business within the Community, provided at least two of them are governed by the laws of different Member States;

- *“company with share capital”* means a company having legal personality, possessing separate assets which alone serve to cover its debts and subject under the national law governing it to conditions concerning guarantees such as are provided for by Council Directive 68/151/EEC²⁹ for the protection of the interests of members and others.

Article 2

Save as otherwise provided in this Directive, each company taking part in a cross-border merger shall be governed, as far as the merger formalities are concerned, by the provisions of national law to which it is subject that apply to mergers of this type of company with other companies with share capital subject to the same national law. The said provisions shall include those concerning the decision-making process relating to the merger and the protection of creditors, debenture holders and the holders of securities other than shares to which special rights are attached, as well as of employees as regards rights other than those governed by Article 14.

29 OJ L 65, 14.3.1968, p. 8.

Article 3

1. The Member States shall provide that each management or administrative organ of each of the merging companies must draw up common draft terms of cross-border merger. The common draft terms of cross-border merger shall include the following particulars:
 - (a) the form, name and registered office of the merging companies and those proposed for the company created by the merger;
 - (b) the ratio applicable to the exchange of securities or shares representing the company capital and the amount of any compensation;
 - (c) the terms for the allotment of securities or shares representing the capital of the company created by the merger;
 - (d) the date from which the holding of such securities or shares representing the company capital will entitle the holders to share in profits and any special conditions affecting that entitlement;
 - (e) the date from which the transactions of the merging companies will be treated for accounting purposes as being those of the company created by the merger;
 - (f) the rights conferred by the company created by the merger on members enjoying special rights or on other holders of securities or shares representing the company capital, or the measures proposed concerning them;
 - (g) any special advantages granted to the experts who examine the draft terms of merger or to members of the administrative, management, supervisory or controlling organs of the merging companies;
 - (h) the statutes of the company created by the merger;
 - (i) information on the procedures by which arrangements for the involvement of employees in the definition of their rights to participation in the company created by the merger are determined pursuant to Article 14.

2. In addition to the items provided for in paragraph 1, the merging companies may, by common accord, include further items in the common draft terms of merger.

Article 4

The Member States shall provide that, for each of the merging companies, the following particulars at least must be published, not less than one month before the date of the general meeting referred to in Article 6, in the manner laid down by the law of each Member State in accordance with Article 3 of Directive 68/151/EEC:

- (a) the form, name and registered office of each merging company and those proposed for the company created by the merger;

- (b) the public register in which the documents of each merging company are filed and their identification number in that register;
- (c) an indication, for each of the merging companies, of the arrangements made for the exercise of the rights of creditors and of any minority shareholders of the merging companies and the address at which complete information on those arrangements may be obtained free of charge.

Article 5

1. An expert report intended for members and made available not less than one month before the date of the general meeting referred to in Article 6 shall be drawn up for each merging company.
2. As an alternative to experts operating on behalf of each of the merging companies, one or more independent experts, appointed for that purpose at the joint request of the companies by a judicial or administrative authority in the Member State of one of the merging companies or of the future company, may examine the draft terms of cross-border merger and draw up a single written report to all the shareholders. Depending on the law of each Member State, such experts may be natural persons, legal persons or companies.

The experts shall be entitled to secure from each of the merging companies all information they consider necessary for the discharge of their duties.

Article 6

1. After taking note of the expert report referred to in Article 5, the general meeting of each of the merging companies shall approve the common draft terms of cross-border merger.
2. The general meeting of each of the merging companies may reserve the right to make implementation of the cross-border merger conditional on express ratification by it of the arrangements decided on with respect to the involvement of employees in the company created by the merger.

Article 7

1. Each Member State shall designate the authorities competent to scrutinise the legality of the merger as regards that part of the procedure which concerns each merging company subject to its national law.
2. In each Member State concerned the competent authorities shall issue to

each merging company subject to that State's national law a certificate conclusively attesting to the proper completion of the pre-merger acts and formalities.

Article 8

Each Member State shall designate the authorities competent to scrutinise the legality of the merger as regards that part of the procedure which concerns the completion of the merger and, where appropriate, the formation of a new company created by the merger where the company created by the merger is subject to its national law. The said authorities shall in particular ensure that the merging companies have approved the common draft terms of cross-border merger in the same terms and that arrangements for employee participation have been determined in accordance with Article 14.

To that end each merging company shall submit to the competent authorities the certificate referred to in Article 7(2) within six months of its issue together with the common draft terms of cross-border merger approved by the general meeting referred to in Article 6.

Article 9

The law of the Member State to whose jurisdiction the company created by the merger is subject shall determine the date on which the cross-border merger takes effect. That date must be after the supervision as referred to in Article 8 has been carried out.

Article 10

The law of each of the Member States to whose jurisdiction the merging companies were subject shall determine, with respect to the territory of that State, the arrangements for publicising completion of the cross-border merger in the public register in which each of the companies is required to file documents.

Article 11

1. A merger carried out as laid down in point (a) of the first indent of Article 1 shall, from the date referred to in Article 9, have the following consequences:
 - (a) all the assets and liabilities of each company being acquired are transferred, by way of universal succession, to the acquiring company;
 - (b) the shareholders of the company being acquired become shareholders of the acquiring company;
 - (c) the company being acquired ceases to exist.

2. A merger carried out as laid down in point (b) of the first indent of Article 1 shall, from the date referred to in Article 9, have the following consequences:
 - (a) all the assets and liabilities of the merging companies are transferred, by way of universal succession, to the new company;
 - (b) the shareholders of the merging companies become shareholders of the new company;
 - (c) the merging companies cease to exist.
3. Where, in the case of a merger of companies covered by this Directive, the laws of the Member States require the completion of special formalities before the transfer of certain assets, rights and obligations by the merging companies becomes effective against third parties, those formalities shall be carried out by the company created by the merger.

Article 12

A cross-border merger which has taken effect as provided for in Article 9 may not be declared null and void.

Article 13

1. Where a cross-border merger by acquisition is carried out by a company which holds all the shares and other securities conferring the right to vote at general meetings of the company being acquired, Articles 3(1)(b) and (c), 5 and 11(1)(b) shall not apply.
2. Where a merger by acquisition is carried out by a company which holds 90% or more but not all of the shares and other securities conferring the right to vote at general meetings of another company, reports by the management or administrative body, reports by an independent expert or experts and the documents necessary for scrutiny shall be required only to the extent that the national law governing either the acquiring company or the company being acquired so requires.

Article 14

Where at least one of the merging companies is operating under an employee participation system and where the national law applicable to the company created by the merger does not impose compulsory employee participation, the participation of employees in the company created by the merger and their involvement in the definition of such rights shall be regulated by the Member States in accordance with the principles and procedures laid down in Article 12(2), (3) and (4) of Regulation (EC) No 2157/2001 and the following provisions of

Directive 2001/86/EC:

- (a) Article 3(1), (2) and (3), (4) first subparagraph, first indent, and second subparagraph, (5), (6) first and second subparagraphs and (7);
- (b) Article 4(1),(2), point (g), and (3);
- (c) Article 5;
- (d) Article 6;
- (e) Article 7(1), (2) first subparagraph, point (b), and second subparagraph, and (3);
- (f) Articles 8 to 12;
- (g) Part 3 of the Annex.

Article 15

Member States shall bring into force the laws, regulations and administrative provisions necessary to comply with this Directive within eighteen months of its publication. They shall forthwith inform the Commission thereof and communicate a table of equivalence between those provisions and this Directive.

When Member States adopt such measures, they shall contain a reference to this Directive or shall be accompanied by such reference at the time of their official publication. The procedure for such a reference shall be adopted by Member States.

This Directive shall enter into force on the twentieth day following that of its publication in the Official Journal of the European Union.

Article 16

This Directive is addressed to the Member States.

Done at Brussels,

For the European Parliament
The President

For the Council
The President

THE IMPACT OF THE PROPOSAL ON BUSINESS WITH SPECIAL REFERENCE TO SMALL AND MEDIUM-SIZED ENTERPRISES (SMEs)

TITLE OF PROPOSAL

Proposal for a Directive of the European Parliament and of the Council on cross-border mergers of companies with share capital

REFERENCE NO

COM(2003) 703

THE PROPOSAL

1. Taking account of the principle of subsidiarity, why is Community legislation necessary in this area and what are its main aims?

In accordance with the principles of subsidiarity and proportionality as laid down in Article 3b of the Treaty, the objectives of the proposed action, namely to facilitate mergers between companies from different Member States, cannot be sufficiently achieved by the Member States acting alone. No one Member State is able to organize the operation in full because it has a dimension which goes beyond national frontiers. These objectives can therefore be achieved only at Community level. The Directive is confined to the minimum required in order to achieve those objectives and does not go beyond what is necessary to that end.

THE IMPACT ON BUSINESS

2. Who will be affected by the proposal?

The scope of the Directive covers all companies with share capital. Besides public limited companies and partnerships partly limited by shares, it includes incorporated private companies and other national forms of company with share capital which offer safeguards as coordinated by Directive 68/151/EEC. The proposal will therefore benefit above all small and medium-sized enterprises (SMEs) as defined in the Commission Recommendation of 3 May 1996.³⁰ Owing to their smaller size and lower capitalisation compared with large enterprises, SMEs are rarely set up in the form of a public limited company but rather in that of a private company. SMEs account for about nine out of ten enterprises, almost three out of ten jobs, and just over one fifth of value added in the EU. The removal of legal obstacles to cross-border mergers will help to internationalise such enterprises' activities as advocated by the Commission in its Third Multiannual Programme for Small and Medium-sized Enterprises in the European Union (1997-2000).³¹ No distinction is made according to sector of activity, size of business or geographical area.

30 Commission Recommendation (COM(1996) 261 final) of 3 May 1996 concerning the definition of small and medium-sized enterprises (OJ L 107, 30.4.1996, p. 4).

31 "Maximising European SMEs' full potential for employment, growth and competitiveness" - proposal for a Council Decision adopted by the Commission on 20 March 1996 (COM(96) 98 final; OJ C 156, 31.5.1996, p. 5).

3. What will business have to do to comply with the proposal?

Companies which wish to merge will basically have to draw up draft terms of cross-border merger and publicise them sufficiently in each Member State concerned. The general meeting of each merging company will have to approve the draft terms. The legality of the procedure will have to be certified by the competent authorities. Measures are provided for in order to protect the rights of creditors and the holders of securities. The completion of the cross-border merger will also have to be sufficiently publicised. As in the case of the European company, a single expert report is permitted, which is likely to reduce costs. Most of the measures proposed already exist in Member States' laws on domestic mergers of companies with share capital and in the measures for implementing Directive 78/855/EEC concerning mergers of public limited liability companies. Responsibility for implementing the proposal will rest primarily with the Member States.

4. What economic effects is the proposal likely to have?

The key provisions of the proposal should allow companies which wish to carry out a cross-border merger to benefit from substantially reduced legal and economic requirements, which are currently highly complex and expensive. This benefit will accrue to all companies with share capital in the EU and should therefore have a favourable impact on employment and competitiveness.

5. Does the proposal contain measures to take account of the specific situation of small and medium-sized firms (reduced or different requirements, etc.)?

The proposal is basically attuned to serving the needs of SMEs, which account for about nine out of ten enterprises, but other companies will also be able to benefit from it on the same terms.

CONSULTATION

6. The present proposal is an appropriate response to the needs which companies have been expressing for many years now, and in particular since progress on the original proposal, which was presented in 1984, came to a halt. Other voices have joined in the chorus, including that of UNICE. The High-Level Group of Company Law Experts recently conducted a wide-ranging consultation exercise which elicited numerous responses and expressions of opinion in favour of the present proposal. The Commission's communication to the Council and Parliament of 21 May 2003 on modernising company law and enhancing corporate governance has likewise been the object of extensive consultations. Under the circumstances, it has not been considered necessary to carry out any further consultations, this time on the final draft, all the more so since they would result in the present proposal's adoption being considerably delayed.

Annex C

Definitions and Technical terms

“Merger” A merger may be defined as a corporate restructuring transaction in which all the assets and liabilities of the acquired company (or companies) are transferred to an acquiring company; the acquired companies then being dissolved without going into liquidation. There are two types of merger: -

- **Merger by acquisition** - where an existing company will effectively absorb the assets and liabilities of one or more existing companies (which will be dissolved) in exchange for shares in the acquiring company being issued to the shareholders of the dissolving companies; and
- **Merger by formation of a new company** - In this case, a newly incorporated company will acquire the assets and liabilities of the dissolving companies in return for the issue of shares to the shareholders of those companies.

“Cross-border merger” - Is a merger transaction involving companies at least two of which are governed by the laws of different Member States.

“Employee participation” - Is a system that exists in some Member States (such as Germany, Austria, Netherlands and Sweden) and gives employees the statutory right to involvement at Board level. GB does not have such a mandatory system. Article 14 does not define what is meant by “participation” but, in Article 2(k) of the ECS Directive, it is defined as the influence of the body representative of the employees and/or the employees’ representatives in the affairs of a company by way of:

- (a) the right to elect or appoint some of the members of the company’s supervisory or administrative organ, or
- (b) the right to recommend and/or oppose the appointment of some or all of the members of the company’s supervisory or administrative organ.

Part (a) of the definition intends to cover employee participation systems like those found in Germany, Sweden and Austria, while part (b) intends to cover the type of participation rights existing in the Netherlands.

Annex D

Partial Regulatory Impact Assessment

New proposal for a Directive of the European Parliament and Council concerning cross-border mergers of companies with share capital.

I. Objective

1. This assessment estimates the costs and benefits of the European Commission proposal for a Directive concerning cross-border mergers.
2. The proposal seeks to establish a framework for cross-border mergers (involving companies from at least two different Member States). The Commission explanatory memorandum indicates that the Directive will be aimed primarily at small and medium-sized enterprises across the European Union. The proposal also seeks to protect employee participation rights where they already exist in the merging company or companies.
3. A merger is a form of corporate restructuring involving dissolution of one or more of the participating companies without liquidation. The shareholders of the dissolving company or companies receive shares in the acquiring or newly created company, which also inherits the assets and liabilities of the dissolving companies. Domestic company mergers are governed by provisions in the Third Company Law Directive agreed in 1978, which was implemented into GB legislation by Part XIII of the Companies Act 1985.
4. The Cross-Border Mergers Directive would introduce a system for cross-border restructuring that did not exist previously. The Commission proposal would apply to both public and private companies registered under the companies' legislation in GB (currently there are approximately 1.8 million such companies). Historically, due to cultural and structural conditions in GB economy, corporate restructuring practice has seen greater use of takeovers rather than mergers. Companies listed on the Stock Exchange in GB usually have shares which are widely held and traded, share owners are readily identified and the market operates against practices which facilitate minority shareholders or a board of directors maintaining control against the interests of shareholders generally. Consequently, market forces can determine the outcome of a takeover bid³². In addition, there are few constraints on cross-border investment in equities within the EU and investors, both institutional and individual, are free to invest in those countries where they wish.

32 As stated in the House of Lords Select Committee on the European Communities on Takeover Bids with Evidence, Session 1995-96, 13th Report.

II. Background

5. A commitment to adopt a Directive on cross-border mergers was identified in the Lisbon Financial Services Action Plan, agreed by Heads of State and Government in 2000 with the aim of creating an integrated capital market across the EU by 2005. This Directive has been under consideration since 1984, although the EU Commission withdrew an initial proposal for the Directive in 2001 as employee participation issues had stalled its progress in the European Parliament. The revised proposal arises as a consequence of recent developments and initiatives in European company law, including: -
- the Commission appointing a High Level Group of Company Law Experts in 2001 who examined, following consultation in 2002, the possibility of facilitating cross-border mergers of EU companies; and
 - adoption of the European Company Statute Regulation, which creates a legal framework for a new form of company, the European Company (SE), and accompanying Directive on employee involvement. The Regulation enters into force on 8 October 2004 and will enable SEs to be formed by cross-border merger.
6. Since publication by the Commission of the present proposal on 18 November 2003, the Department of Trade and Industry (DTI) has informally consulted with representatives from organisations including the Confederation of British Industry, Financial Services Authority, Investment Management Association, the Law Society, the London Stock Exchange and National Association of Pension Funds. Whilst identifying some degree of support for the principles underlying the Directive, this informal consultation exercise also revealed concerns with regards to the proposed provisions in the Directive relating to employee participation. Some viewed the employee participation provisions as potentially burdensome for companies, disproportionate, too rigid and could result in lengthy delays that may deter companies from using the merger procedure under the Directive (the employee participation provisions are considered in more detail at paragraphs 22-39 below).

III. Effects of the measure

7. One of the main features of the Directive is cross-border merger transaction provisions covering all companies with share capital similar to those established under the Third Company Law Directive for public companies involved in domestic merger transactions. The Directive has the potential to impact all companies with share capital, which will include public and private limited companies.

8. Rules are included on specific cross-border elements of the merger transaction such as parallel certification in different Member States where the formalities of the merger have been completed. There are a number of protections for shareholders and others proposed, including a requirement for a shareholders meeting to agree the merger and publicity provisions. Once the merger takes effect it cannot be declared null and void which will provide certainty for companies. The Directive also includes provisions for entering into negotiations on employee participation rights (a system of mandatory representation of employees on the board of the company) where a merging company has participation rights but the law of the Member State in which the acquiring or new company will be situated does not have such rights.

IV. Risk assessment

9. The Directive introduces a new option for cross-border merger restructuring procedures. At present, companies are able to restructure cross-border through the use of a number of mechanisms including takeovers. If companies elect to use the cross-border restructuring procedure set up under this Directive they will be bound by the Directive's provisions. As using the cross-border merger procedure will be entirely voluntary, only companies that foresee real commercial benefits will take advantage of the framework introduced by the Directive. **In addition, it is considered that GB registered companies will not be placed at a competitive disadvantage by two or more companies merging in other Member States. Comments are welcomed on this assessment.**

V. Options for Implementation

10. (i) **Do nothing:** The Directive is applicable throughout the EEA and will require implementation once agreed. It is not possible therefore, to take no action.
- (ii) **Implementing the Directive:** Final details of what will need to be implemented will be determined in the ongoing EU negotiations. Currently, issues under discussion include the types of companies that will be able to use the provisions under the Directive and how employee participation provisions will apply to the merged company. The DTI will wish to consider, after further consultation, implementing the Directive by following the approach in current legislation for domestic mergers. Provisions inserted into Part XIII of the Companies Act 1985 implemented the Third Directive dealing with domestic mergers and GB companies will be aware of the procedures under these provisions. Consideration will be given to implementing the Directive via secondary legislation

under section 2 of the European Communities Act 1972. In addition, consideration will be given to any issues arising from practical experience in relation to the European Company Statute, which will introduce similar cross-border merger provisions for European Companies on 8 October 2004.

VI. Benefits

11. There is no current EU regulatory structure governing cross-border mergers and it is assumed that the principal benefits likely to arise from the Directive are through encouraging cross-border merger activity, particularly by small businesses. The DTI is seeking comments through the consultation process on whether the activity should benefit small companies and assist in furthering Single Market objectives.
12. The likely take up of the cross-border merger procedures by GB companies is not known at this point. However, it is understood that the merger procedure (involving dissolution of one or all of the participating companies) is relatively little used within GB at present and that the more common form of company reorganisation is by means of a takeover, as stated above. Takeovers do not lead to the dissolution of the acquired company, but a transfer of share ownership.
13. The Office of National Statistics provides statistics covering all types of merger and acquisition activity³³ ('M&A activity') in the EU. In 2003, 47 UK companies participated in cross-border M&A activity in the EU whilst 25 non-UK EU companies participated in cross-border M&A activity in the UK. Domestically, there were a total of 558 'mergers and acquisitions' by UK companies. However, these statistics do not differentiate between types of M&A activity and include restructuring mechanisms other than mergers, such as takeover bids. The Directive may:-
 - (i) add to the total number of cross-border mergers and acquisitions within the EU by providing a restructuring facility for M&A activity that would not otherwise have taken place; or
 - (ii) provide alternative options for M&A activity in addition to existing restructuring mechanisms.
14. Evidence from other Member States indicates that merger procedures are more frequently used for corporate restructuring than takeovers due to tax,

33 Sourced from national statistics, 'First Release' published 4 May 2003, 'Mergers and acquisitions involving UK companies' - the scope of transactions covered goes further than the Directive and is broader involving any transaction where a company acquires a controlling interest in the acquiring company, or to any deal where ultimate ownership remains in the UK.

cultural and other financial reasons. In addition, corporate restructuring takes the form of strategic alliances (at the level of subsidiaries) as these are perceived to be less costly, risky and in some Member States this makes it easier to comply with accounting regulations. The European Commission states that cross-border merger transactions are currently not possible in Austria, Denmark, Finland, Germany, Greece, Ireland, the Netherlands and Sweden³⁴. Under the new proposed Directive, such transactions would be allowed across the EU. **It is probable that use of the Directive in other Member States will be greater than that in the UK, and comments are welcomed on this point.** The facilitation of cross-border mergers would, therefore, promote choice and competition between corporate forms and procedures.

VII. Equity and fairness

15. The cross-border mergers Directive is voluntary and only those companies, which perceive that there is an advantage to them, will consider merging cross-borders. The provisions on employee participation may be seen as unfair to private companies (as private companies rarely have employee participation arrangements). However, from the perspective of a GB private company taking part in a cross-border merger, employee participation negotiations would only arise where participation arrangements existed in the other merging company and where the acquiring or new company would be registered in GB or another Member State which did not have a mandatory employee participation regime. It is therefore considered that cases where private companies choose this option, will be rare.
16. It is recognised that a consequence of introducing the Directive may be a shift in restructuring activity patterns (for instance from takeovers to mergers), however it is assumed that any company that decides to use the merger procedure would do so because they anticipated real commercial benefit to them.

VIII. Costs Estimates

17. It is too early to identify detailed financial implications, as the Directive is proceeding through the negotiation process and we intend for the consultation to provide detailed analysis. Post negotiation, DTI will consult further on the practicalities of implementation. **The key negotiation points concern the scope of the Directive (the types of company to which it should apply) and employee participation. Comments are, therefore, welcomed on**

34 Taken from EC 'frequently asked questions' - http://europa.eu.int/comm/internal_market/en/company/company/mergers/mergers_en.htm

the likely use of the Directive by, in particular, small businesses and any employee participation cost implications to them. As the Directive is voluntary, no company is obliged to use the procedure provided by it and consequently there will be no mandatory costs imposed on business. In the event that a company chooses voluntarily to adopt the cross-border merger procedure, the resulting anticipated benefits such as increased strength in the market and enhanced competitiveness should outweigh the costs involved. These expected costs would include legal costs (instructing lawyers to draft terms), administrative costs (for publishing the terms) and business costs (associated with trading in another member state). An approximate guide to these legal and administrative costs is set out below.

18. There appear to be three stages in deciding to proceed with a cross-border merger. Firstly, a senior employee would decide whether a cross-border merger would be a viable option, the company board would need to consider the options and subsequently, legal advice would be sought. The cost of such legal advice would clearly vary on a case by case basis and be determined, at least initially, on the type and extent of the advice sought by the company.
19. Any attempt to cost the above exercise is fraught with difficulties. However, in respect of the first stage, the cost of a manager spending two days (sixteen hours) considering whether there was a case for participating in a cross-border merger is estimated to be around £400³⁵. If it is assumed (on the basis of total UK companies involved in restructuring activity within the EU (see paragraph 15)) that 50 of the 1.8 million companies referred to in paragraph 4 above undertook this exercise the cost to GB business would be £20,000. In respect of the second stage, a company board of 12 members considering the issue for two hours would represent a further 24 hours of costs with an estimated total cost of £600³⁶. If it is assumed that the same number of companies undertook this exercise the cost to GB business would be £30,000. Trying to assess legal costs is even more difficult since, as noted above, they would clearly vary on a case-by-case basis. However, the cost of a solicitor spending one day (eight hours) considering draft merger terms and conditions is estimated to be £2,400³⁷. If it is assumed again that 50 of the 1.8 million companies undertook this exercise the cost to GB business would be £120,000. If a cross-border merger resulted in greater flexibility or

35 In 2003, the average hourly pay, excluding overtime, of a manager in Great Britain was £20. 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, £20 x 1.3 = £26. Source: New Earnings Survey (NES) 2003.

36 The same figures as denoted in footnote 35 above have been used in estimating the costs of members of the board.

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

benefits, in single market terms, it is likely that the procedure would be adopted.

20. There may also be additional costs involved with the employee participation aspects of the Directive. Where participation arrangements exist in one or more of the merging companies, but the law of the Member State applicable to the company created by the merger does not require such rights, there will need to be a process of negotiation to resolve how employee participation arrangements should be dealt with in the newly formed or acquiring company. After negotiation, there may be additional costs in relation to employee participation at board level.
21. The cost implications of employee participation were dealt with in the context of the Directive, regarding employee involvement in an SE, which supplements the European Company Statute (ECS) Regulation. The employee participation provisions contained in Article 14 of the Commission's proposal for the cross-border mergers Directive are based on those contained in ECS Directive. The examples set out below were used in the Regulatory Impact Assessment for the ECS, although that assessment referred to provisions for informing and consulting employees, as well as participation. Costs have been adjusted to take into account latest available data and information. The proposal for a cross-border mergers Directive does not include any rules on information and consultation, which are already covered by other legislation. Full details of the costs relating to the ECS Directive can be found in the Regulatory Impact Assessment that was included in the European Company Statute consultation document published in October 2003 by the Department of Trade and Industry ("Implementation of the European Company Statute: The European Public Limited-Liability Company Regulations" URN 03/1279). The consultation document is available at the DTI website: <http://www.dti.gov.uk/cld/condocs.htm>.

Employee participation costs

22. In the event that companies decided to use the cross-border merger procedure, it is likely that, where applicable, the principal additional costs would come from any employee participation arrangements. However, the voluntary nature of cross-border merging, as well as the many different circumstances of the companies involved, make it very difficult to come up with an estimate of the overall costs. It must be stressed that the employee participation provisions would only apply where one of the merging companies already had existing participation arrangements (effectively, employee representation on the board).
23. There are a variety of approaches amongst Member States to employee

participation issues. Some Member States do not impose mandatory employee participation provisions (such as Spain, Ireland and the UK). In Member States that do have statutory participation rights, the application of such provisions is, in general, either limited to certain types of company and/or only applies where the number of employees reaches a particular threshold (for example, employee participation rules apply in German companies if there are more than 500 employees). Since the Directive is aimed at small and medium-sized companies, and employee participation provisions will only apply where participation already existed in one of the merging companies, the costs associated with the employee participation provisions may only apply in a minority of cross-border merger transactions.

24. Some illustrative costs are set out below, based on two companies of a similar size that intend to merge and register as a GB company. In this example, one is a GB company with no employee participation and the other is based in another EU country and is subject to participation. Costs may be higher if there are more than two companies involved. The examples used below assume that there are no subsidiaries and the employees of each company are located in each of their two respective Member States. Specific provisions from the ECS Directive are applied directly to Article 14 of the cross-border mergers proposal and are referred to in the proposal, and in the examples below, as provisions of the ECS Directive.

25. For the purpose of agreeing the arrangements for employee participation that will apply to the merged company, a Special Negotiating Body (SNB), made up of employee representatives from the merging companies and any “concerned” subsidiaries, must be established. Any expenses relating to the functioning of the SNB, and to the negotiations in general, must be borne by the merging companies (this may include the cost of up to one “expert” to assist the SNB). The SNB and management have 6 months, extendable to 12 months, in which to reach a voluntary agreement on employee participation (pursuant to Article 4 of the ECS Directive). There are two possible outcomes:
 - i) the SNB and the management draw up a voluntary agreement for employee participation, under Article 4 of the ECS Directive; or
 - ii) no voluntary agreement is reached by the end of the negotiating period but the merging companies still wish to merge. In such a case, the standard “fallback” rules, contained in Part 3 of the Annex to the ECS Directive, will apply.

Ballots to elect SNB members and number of SNB representatives

26. A ballot should usually be conducted to elect SNB representatives for the GB employees; although, the Government intends to allow consultative

committees, where they exist and certain conditions are met, to appoint members. Separate ballots may need to be conducted in each Member State where the participating companies or subsidiaries have employees although this will not always be the case. In some Member States (such as Germany), existing works council members may simply be appointed as SNB members and no ballots would be held.

27. The cost of conducting a ballot to elect the GB SNB members is estimated to be around £13,650³⁸. There would be no additional balloting cost in the other Member States where the works council is used to nominate its SNB members.
28. The rules for the composition of the Special Negotiating Body (SNB) depend on a variety of factors including the number of merging companies or “concerned” subsidiaries and in how many Member States the employees are located and in what proportion etc. The method of determining the number of SNB members in the Directive implies that there will always be a minimum of 10 SNB members and currently, with the 28 countries of the EEA covered by the Directive on employee involvement, an absolute maximum of 37.

Costs of a special negotiating body meeting

29. Assuming that the merging companies have a total of 50,000 employees, an SNB might have 10 employee representatives and 6 management representatives. The costs of this meeting would include the opportunity cost of the workers’ and employers’ time, travel costs, the cost of the venue and interpreter costs. It is estimated that the costs for one meeting would be about £23,000³⁹.

Illustrative costs

30. Under the Commission proposal, GB companies will only need to enter into

38 This is the cost for a ballot in GB only. For full details of a breakdown of this figure, see the annex of “Implementation of the Regulations on European Works Councils - Regulatory Impact Assessment”. Source: <http://www.dti.gov.uk/er/emp-ria.pdf>

39 The cost of worker time is taken to be £115 per day and the cost of management time is £200. This is based on earnings information multiplied by 1.3 to take into account non-wage costs. Source: New Earnings Survey 2003. It is assumed that each worker and each manager needs to dedicate two days per meeting. It is estimated that travel will cost £10,000, interpretation £5,000 and the venue £3,000. This is based on the findings of the study by T Weber, P Foster and K Levent Egriboz entitled “Costs and Benefits of European Works Councils Directive” Employment Relations Research Series No 9 <http://www.dti.gov.uk/er/emar/camp.pdf>. It is assumed that the costs are evenly distributed between the companies (ie in the two company example, the GB company would therefore pay half of this cost).

negotiations for employee participation arrangements if they intend to merge with a company that is subject to employee participation and then register in a Member State that does not impose statutory participation rules. For example, where a GB company merges with a Swedish company that has employee participation and intends to register in GB. As mentioned, there are two possible outcomes - either a negotiated agreement or, where negotiations fail, the application of the standard rules (which extend the highest level of participation that existed in any of the merging companies to all of the merged company).

31. Where negotiations are relatively straightforward, only two SNB meetings may be necessary for the representatives to agree employee participation arrangements for the merged company. This would cost about £46,000.
32. Where it takes 4 SNB meetings to come to a voluntary agreement on employee participation, there would be a cost of £92,000.
33. It is assumed that failure to reach a voluntary agreement is time consuming and could take 6 to 8 SNB meetings, with a cost of about £140,000 to £180,000.

Participation at board level

34. If one of the merging companies already has worker participation on the company board, there will need to be at least the same level of participation on the new company board (unless the SNB take a two-thirds majority decision to reduce, or even abolish, employee participation in the new company). Since there is no tradition of employee participation in GB, the possible costs involved have been estimated using the German model as an example.
35. The maximum percentage of representatives is likely to be 50% of the board as this is the maximum that applies in Germany; it is doubtful that this percentage would be exceeded. In this example it is assumed that there are two worker representatives on the board of the company in the non-GB company and that the SNB decides that there should be four - two from each country. This would mean an extra two worker representatives attending maybe 12 meetings per year, which take up one day of each representative's time.⁴⁰ The cost of travel has been included, but not interpreter and venue

⁴⁰ It is assumed that the GB worker representative needs one day to read the papers, travel to and attend the meeting. Costs of consulting employees are already included in the costs of extra information and consultation.

costs (since these costs will already have been included). It is estimated that this will cost about £15,000 per year.

36. In Germany, a proportion of the employee representatives on the boards of companies may be full time union representatives who are paid by the company for this purpose. If this model were followed for the boards of companies that participate in a cross-border merger, there would be no opportunity costs to companies of employee time for these representatives.
37. It is sometimes argued that worker participation on boards can slow down decision-making and hence reduce companies' competitive edge. However, evidence from Japanese companies with works councils in Germany does not show this to be the case.⁴¹ Accordingly, no costs have been factored in for longer decision-making processes.
38. Once the employee participation arrangements have been put into place, compliance is likely to follow similar rules and procedures to those set out in other employee involvement legislation such as the forthcoming European Company Statute Regulations and the existing Transnational Information and Consultation of Employees (TICE) Regulations, which implement the European Works Council Directive. There will therefore be costs to employers if a complaint is brought before the Central Arbitration Committee (CAC) or an Employment Tribunal.
39. The costs of appearing at the CAC is estimated to be £4,713⁴² and consists of the average cost of a CAC case together with the cost of 2 days of management time and 1 day of employee representative time. The costs of appearing at an Employment Tribunal are £2,910 and consist of £2,000 for the employer and £910 for the Employment Tribunal Service (ETS).⁴³

Enforcement costs

40. Enforcement of legislation dealing with employee participation is the responsibility of the Department of Trade and Industry. There will also need to be enforcement of the procedure and review and confirmation of the legality of a cross-border merger.

41 Source: S Nakano "Management Views of European Works Councils: A Preliminary Survey of Japanese Multinationals" 1999 European Journal of Industrial Relations Volume 5 Number 3 pages 307-326.

42 This includes the cost to the CAC of £4,198 and the cost to the employer of around £515.

43 Source: Findings from the 1998 Survey of Employment Tribunal Applications, ETS and Acas.

IX. Monitoring and review

41. No specific review of the Directive's provisions is provided for within the Commission Proposal itself. The Department has consulted on the implementation of the European Company Statute Regulation, which comes into force on 8 October 2004, allowing for European companies to be formed by cross-border merger. Additionally, the provisions of the Companies Act 1985 relating to domestic mergers remain under consideration as part of the Department's ongoing consideration of fundamental reform of company law.

X. Small firms' impact test

42. The key point is that merging cross-border will be voluntary and no costs will be imposed on small firms unless they opt to use the merger procedure provided by the Directive. The DTI through the consultation document intends to consult with small business on the likely uptake of the Directive and any arising issues to small business. DTI small business services have been consulted and they are content to proceed with the consultation on this basis.
43. Although estimating costs on small business is difficult, in deciding whether or not to proceed with a cross-border merger transaction, we have estimated that the likely legal costs will be £2400 based on a solicitor spending one day (eight hours) considering draft merger terms and conditions⁴⁴, and administrative costs that would total £400 (based on 1 director reviewing and deciding to proceed in 2 days). **Comments are welcomed on the estimated anticipated costs to small business if they proceed with a cross-border merger.**
44. As stated above, it is not anticipated that there will be employee participation costs to small business, as small businesses rarely have any employee participation. It is anticipated that the impact to small business will be negligible, however if the consultation responses indicate otherwise, we will consider any points that may arise.

XI. Competition assessment

45. The competition filter has been applied. It has been concluded that the Directive has a potential impact on all GB companies, all market sectors and that the distribution of market shares within those sectors could be affected

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

by the new procedure if companies choose to use it. It is considered that the Directive will not give rise to disproportionate costs of entry or administrative costs for either small or large business. As the Directive is voluntary, only companies which perceive real business advantage will elect to use the procedures. The Directive is not anticipated to restrict innovation in sectors characterised by rapid technological change and would not impair freedom to provide services.

46. The proposed Directive will affect all markets since the companies that may participate in a cross-border merger are not restricted to any particular sector. This Directive will not impose additional costs - either set-up or ongoing - on any companies nor restrict the ability of companies to choose the price, quality, range or location of their products. It is anticipated that the legislation will not affect competition, either positively or negatively. It is possible that the legislation will have an effect on market structure since the companies formed by cross-border merger could (but not necessarily would) lead to a smaller number of GB registered companies.

XII. Summary and Recommendation

47. The proposed Directive seeks to establish a framework for cross-border mergers where such a process was not provided for previously. The overall impact of the new Directive is unlikely to have significant consequences for business, however it will provide a useful additional tool for corporate restructuring within the internal market. The Government supports the objective of agreeing a cross-border mergers Directive and remains committed to extending the opportunities for corporate restructuring across the EU as crucial to the Single Market. It is imperative that the Directive, once agreed, offers practical solutions to the issues of cross-border restructuring for businesses within the EU, provides legal certainty and avoids unnecessary burdens and constraints on business. The DTI is seeking further views on this assessment in the consultation.

Annex E

Code of Practice on Consultations

The Consultation Code of Practice Criteria

1. Timing of consultation should be built into the planning process for a policy (including legislation) or service from the start, so that it has the best prospect of improving the proposals concerned, and so that sufficient time is left for it at each stage.
2. It should be clear who is being consulted, about what questions, in what timescale and for what purpose.
3. A consultation document should be as simple and concise as possible. It should include a summary, in two pages at most, of the main questions it seeks views on. It should make it as easy as possible for readers to respond, make contact or complain.
4. Documents should be made widely available, with the fullest use of electronic means (though not to the exclusion of others) and effectively drawn to the attention of all interested groups and individuals.
5. Sufficient time should be allowed for considered responses from all groups with an interest. Twelve weeks should be the standard minimum period for a consultation.
6. Responses should be carefully and open-mindedly analysed, and the results made widely available, with an account of the views expressed, and the reasons for decisions finally taken.
7. Departments should monitor and evaluate consultations, designating a consultation co-ordinator who will ensure the lessons are disseminated. The complete code is available on the Cabinet Office's web site, address <http://www.cabinet-office.gov.uk/servicefirst/index/consultation.htm>.



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