

# **Implementation of the EU Directive on Takeover Bids**

## **Guidance on changes to the rules on company takeovers**

**Effective from: 20 May 2006**

This document provides:-

- Background on the EU Directive on Takeover Bids (“the Takeovers Directive”);
- A guide to regulations making changes to the takeover regulatory regime;
- Information about changes that affect the Panel on Takeovers and Mergers (“the Panel”) and the City Code on Takeovers and Mergers (“the Takeover Code”); and
- Information about further changes to be made by the Companies Act 2006.

The guidance has no legal force but it is intended to help business understand the main features of the changes made and the circumstances in which they apply. Those affected should refer to the Takeovers Directive (Interim Implementation) Regulations 2006 (“the Regulations”), Part 28 of the Companies Act 2006 and the Takeover Code for a full statement of the legal requirements.

Whilst every effort has been made to ensure that the information in this document is accurate, the Department of Trade and Industry cannot accept liability for any errors, omissions or misleading statements in that information and readers are advised to seek legal advice as to the application of the above legislation to their individual circumstances.

**Department of Trade and Industry**  
**Revised February 2007**

## **INTRODUCTION – THE TAKEOVERS DIRECTIVE**

The Takeovers Directive<sup>1</sup> was adopted on 21 April 2004 and had to be implemented by all Member States<sup>2</sup> no later than 20 May 2006.

The Takeovers Directive lays down, for the first time, minimum EU rules concerning the regulation of takeovers of companies whose shares are traded on a regulated market<sup>3</sup>. The Takeovers Directive is one of the measures adopted under the EU Financial Services Action Plan. It aims to strengthen the Single Market in financial services by facilitating cross-border restructuring and enhancing minority shareholder protection.

The Takeovers Directive contains:-

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

## **THE GOVERNMENT’S APPROACH TO IMPLEMENTATION OF THE TAKEOVERS DIRECTIVE**

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<sup>1</sup> European Directive on Takeover Bids (2004/25/EC)

<sup>2</sup> Member States includes the 27 Member States of the European Union together with the 3 States that make up the European Economic Area.

<sup>3</sup> Regulated markets are defined by article 4(1)(14) of Directive 2004/39 EC. A financial market (e.g. a Stock Exchange) may ask to be designated as a “regulated market” if it meets conditions laid down. A list of regulated markets is situated on the website of the Financial Services Authority at <http://fsahandbook.info/FSA/html/handbook/SUP/17/Annex5>

## **A. Establishing a regulatory framework for a body supervising takeover bids**

Since 1968, takeover regulation in the UK has been overseen by the Panel<sup>4</sup>. The Panel administers rules contained in the Takeover Code<sup>5</sup>, which historically had had no legal force. The Takeovers Directive requires that certain of the regulatory activities of the Panel be placed within a legal framework.

The Government recognised the considerable strengths of the system of takeover regulation overseen by the Panel, including:-

- Flexibility, speed and certainty in decision-making;
- Independence and regulatory autonomy;
- Principles-based regulation;
- Involvement of key City and business participants in developing takeover rules and the regulatory framework;
- Professional expertise in regulatory activities, notably through Panel membership and secondments; and
- Consensual approach to regulation amongst those involved in the markets.

The Government wishes to preserve these core characteristics of takeover regulation. It is also necessary to ensure proper legal certainty and confidence in the new legal framework created by the Takeovers Directive. The Government's implementing measures, therefore:-

- a.) Provide statutory underpinning to the regulatory activities of the Panel; and
- b.) Leave the Panel considerable scope to decide its internal structures and operational framework.

The Panel will remain an unincorporated body and, as such, will continue to have rights and obligations under common law, which will be supplemented by the relevant legislative provisions. The Panel will have power to make rules in relation to takeover regulation. It will continue to make rulings on the interpretation, application and effect of the Takeover Code and to give directions.

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<sup>4</sup> Further information about the Panel is available on the Panel's website at <http://www.thetakeoverpanel.org.uk/new/>.

<sup>5</sup> The City Code on Takeovers and Mergers. Copies of the Takeover Code are available on <http://www.thetakeoverpanel.org.uk/new/>.

## **B. Restricting barriers to takeovers**

The Takeovers Directive seeks to override certain steps that may be taken by companies both prior to and during a takeover bid which have the aim of frustrating a bid:-

a.) Pre-bid defences (known in the Takeovers Directive as “breakthrough provisions” and contained in Article 11) - Such defences include differential share structures under which minority shareholders exercise disproportionate voting rights; limitations on share ownership and restrictions on transfer of shares set out in the company’s articles or in contractual agreements. As permitted by the Takeovers Directive, the Government has decided not to apply the breakthrough provisions in all cases but instead to allow companies with voting shares traded on a regulated market to opt in to these provisions should they wish to do so.

b.) Post-bid defences (article 9) – Management of a target company are prevented from taking action to frustrate a bid (such as sale of key assets of the company) without the approval of shareholders at the time of the bid. The rules banning this type of defensive action are contained in the Takeover Code.

## **C. New disclosure requirements**

Provisions related to disclosures by companies are contained in Part 7 of the Companies Act 1985 (in the case of Northern Ireland, Part 8 of the Companies (Northern Ireland) Order 1986). That Part will be extended to include the new disclosure requirements in the Takeovers Directive, concerning matters such as the share and control structures of companies which will have to be included in the directors’ report. These provisions will only apply to companies whose shares are traded on a regulated market.

## **D. Minority shareholders following a takeover**

The concepts of “squeeze out” and “sell out”, which have long been a feature of national company law,<sup>6</sup> are designed to address the problems of, and for residual minority shareholders following a successful takeover bid. Squeeze out rights enable a successful

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<sup>6</sup> See Part 13A of the Companies Act 1985 (Part 14A of the Companies (Northern Ireland) Order 1986).

bidder to purchase compulsorily the shares of remaining minority shareholders who have not accepted the bid. Sell out rights enable minority shareholders to require the majority shareholder to purchase their shares.

The rules in the Takeovers Directive relating to squeeze out and sell-out are broadly consistent with existing provisions, although they do require some amendments to Part 13A of the Companies Act 1985 (Part 14A of the Companies (Northern Ireland) Order 1986). The Government has decided to apply these amended provisions to all companies and all bids within the ambit of Part 13A (Part 14A in Northern Ireland) whether or not the Takeovers Directive requires this.

The Government has also taken the opportunity to adopt some recommendations of the Company Law Review in relation to Part 13A (Part 14A in Northern Ireland) (see below).

## **METHODS OF IMPLEMENTATION**

### **A. The Companies Act 2006 (Part 28)**

The main implementing provisions are contained in Part 28 (sections 942-992) of the Companies Act 2006. More information about the Act is available on the DTI website at: <http://www.dti.gov.uk/bbf/co-act-2006/index.html>.

This includes a link to the Act and the explanatory notes. The Act received Royal Assent on 8 November 2006.

#### When will the provisions on takeovers be brought into force?

A draft commencement Order, the Companies Act 2006 (Commencement No.2, Consequential Amendments, Transitional Provisions and Savings) Order 2007 was laid before Parliament in draft on 8 February 2007 and, if approved by both Houses, will come into force on 6 April 2007. This would commence the provisions of Part 28 of the Act.

#### Will the Companies Act 2006 apply to the whole of the United Kingdom?

Yes, the provisions will apply throughout Great Britain and Northern Ireland.

### How will the Companies Act 2006 provisions be enforced?

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

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

### Do the takeovers provisions of the Companies Act 2006 apply to unregistered companies?

Alongside the draft commencement Order, the Companies Acts (Unregistered Companies) Regulations 2007 were laid. These regulations (which have already been made, because they do not require approval in draft) extend certain provisions of the Companies Act 2006 regarding takeovers to unregistered companies and are designed to give full effect to implementation of the Takeovers Directive together with commencement of Part 28 of the Act. The Regulations will come into force on 6 April 2007. The Panel will also be able to make rules concerning takeovers of unregistered companies.

## **B. The Takeovers Directive (Interim Implementation) Regulations 2006 (S.I. 2006/1183)**

### Why were interim regulations necessary?

The Companies Act 2006 had not completed the Parliamentary process by 20 May 2006, when the Takeovers Directive had to be implemented. Regulations were therefore made under powers in the European Communities Act 1972, to make the necessary changes on an interim basis. The Regulations came into force on 20 May 2006, to meet the implementation deadline for the Takeovers Directive. They will cease to have effect as soon as the relevant provisions in the Companies Act 2006 come into force.

### What types of takeovers will the Regulations apply to?

The Regulations apply only to transactions to which the Takeovers Directive applies. The Takeovers Directive applies to takeover bids for companies which are:-

- a.) governed by the laws of Member States; and
- b.) traded on a regulated market.

The Regulations apply throughout Great Britain and Northern Ireland.

### What provisions do the Regulations contain?

The Regulations substantially mirror provisions contained in Part 28 of the Companies Act 2006 in relation to takeover transactions covered by the Takeovers Directive (but see below for crucial differences between the Regulations and the Act).

### Do the Regulations contain all the rules that apply to takeovers?

No. As at present, the majority of the rules relating to takeovers will be contained in the Takeover Code, which is adopted by the Regulations. The Panel has consulted<sup>7</sup> on the changes that needed to be made to the Takeover Code to ensure that the rules meet the requirements of the Takeovers Directive. Arising from that consultation, all necessary changes to the Takeover Code had been adopted and came into effect on 20 May 2006.

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<sup>7</sup> A copy of the Response Statement ( "The Implementation of the Takeovers Directive – Statement by the Panel and the Code Committee following the external consultation process on PCP 2005/5) issued on 21 April 2006 and setting out the changes made is available on the Panel's website <http://www.thetakeoverpanel.org.uk/new/consultation/DATA//RS200505.pdf>.

The Regulations set out the law relating to the position of minority shareholders following a successful takeover (“squeeze-out” and “sell-out”) as amended by the Takeovers Directive. Additionally, the Regulations list the information that the Takeovers Directive requires to be included in a directors’ report (in addition to that already required by Part 7 of the Companies Act 1985 (Part 8 of the Companies (Northern Ireland) Order 1986)).

How will transactions which may affect the ownership or control of companies, but are not governed by the Regulations, be regulated?

The Panel currently regulates various types of transactions that the Takeovers Directive does not apply to. These include takeovers of public companies whose shares are not traded on a regulated market and mergers. The Panel will continue to regulate these transactions following the coming into force of the new Regulations in accordance with the rules in the Takeover Code. The Regulations do not, however, give statutory recognition to the Takeover Code in respect of such transactions. Therefore, certain new powers, such as the right for the Panel to enforce its rulings by application to court, contained in the Regulations do not apply to such transactions.

How will the Regulations be enforced?

The Regulations will be enforced in the same way as the Companies Act 2006 provisions on takeovers (see above).

From where are the Regulations available?

The Takeovers Directive (Interim Implementation) Regulations 2006 (S.I. 2006/1183) are available on the website of the Office of Public Sector Information:  
<http://www.opsi.gov.uk/stat.htm>.

What are the main differences between the provisions on takeovers contained in the Companies Act 2006 and the Regulations?

There are four main differences:-

### *a.) Types of transactions*

The Regulations only apply to takeover bids covered by the Takeovers Directive. The Companies Act 2006 provisions will apply more widely to other types of transactions which may have an effect on the ownership or control of companies, such as takeovers of public companies whose shares are not traded on a regulated market and mergers.

### *b.) Panel's Rule-making Power*

In regulations made under the European Communities Act 1972, it is not possible to give the Panel power to make and amend rules which have statutory effect. The Panel will not, therefore, during the period between 20 May 2006 and the entry into force of the relevant provisions of the Companies Act 2006, be able to adopt amendments to the Takeover Code in so far as they relate to matters contained in the Takeovers Directive.

The Companies Act 2006 includes a rule-making power which, once it becomes law, will enable the Panel to make and amend rules both in relation to transactions covered by the Takeovers Directive and other types of transactions which may have an effect on the ownership or control of companies.

### *c.) Squeeze-out and sell-out provisions*

The Regulations only contain squeeze-out and sell-out provisions necessary to give effect to the Takeovers Directive. Further unrelated changes being made by the Companies Act 2006 to reflect recommendations made by the Company Law Review are not included. (Note: The provisions at Part 28 (Chapter 3) of the Companies Act 2006 restate Part 13A of the Companies Act 1985 in a clearer form. In doing so, they also make important changes to reflect the need to ensure compliance with the Takeovers Directive and the decision to accept some recommendations of the Company Law Review.)

### *d.) Offences*

Certain offence provisions under the Regulations (for instance, in relation to unlawful disclosure of information subject to secrecy provisions) apply in a different way to those under the Companies

Act 2006. They are restricted to matters covered by the Takeovers Directive. Similarly, the maximum penalties that may be imposed under the Regulations are restricted by the powers in the European Communities Act 1972.

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