The Panel on Take-overs and Mergers

Report on the Year ended 31st March, 1977

MEMBERSHIP OF THE PANEL

Lord Shawcross (Chairman)	Nominated by the Governor of the Bank of England
Sir Alexander Johnston (Deputy Chairman)	Nominated by the Governor of the Bank of England
The Hon. John Baring	Chairman, Accepting Houses Committee
E. H. Bond	Nominated by the Confederation of British Industry
N. P. Goodison	Chairman, The Stock Exchange
W. G. Haslam	Chairman, British Insurance Association
D. A. Hunter Johnston	Chairman, Association of Investment Trust Companies
I. G. Kennington	Chairman, Issuing Houses Association
E. W. I. Palamountain	Chairman, Unit Trust Association
K. G. Smith	Chairman, National Association of Pension Funds
A. F. Tuke	Chairman, Committee of London Clearing Bankers

Lord Cross	Chairman of the Appeal Committee of the Panel

THE PANEL EXECUTIVE

D. C. Macdonald	Director General
P. R. Frazer	Deputy Director General
T. P. Lee	Assistant Director General and Secretary
F. J. P. Madden	Assistant Director General
P. R. Hamilton	
J. M. Holt	
R. A. Wade	
Miss M. J. Tomlinson	
Miss M. C. Langley	

FOREWORD

Statistics relating to the Panel's work give an inadequate reflection of the effectiveness of the system of self regulation in the securities market. Thus it might be thought by some that the comparatively small number of occasions on which the full Panel has had to consider matters arising out of take-over transactions is some indication of inactivity on the Panel's part. Almost the opposite is the case. The fact is that the provisions of the City Code are well known to practitioners in the securities industry and that the Code, with the Panel behind it, has become wholly accepted as an authoritative statement of the Rules and Principles which must be followed. The Panel executive has continued to be kept very busy throughout the year advising on the application of the Code to particular cases and, with their assistance known to be available and constantly made use of, the system of self regulation of this aspect of the City's affairs has on the whole operated with a very remarkable degree of efficiency.

This is not of course to say that nothing improper occurs in take-over transactions. No doubt occasional cases escape notice. No doubt in some instances non-statutory investigations conducted by the Panel with the degree of expedition which is itself necessary to the utility of the system, may fail to uncover matters which a much more laborious exploration, extending over many months or years and with statutory powers of interrogation, might eventually discover–but so late that their discovery sometimes has little relevance for shareholders. It must, however, be emphasised that the Panel's jurisdiction, as in any system of self regulation, depends upon the most loyal acceptance of its disciplines. The Panel expects complete frankness and the avoidance of any equivocation or deception from those with whom it deals. The obligations of professional advisers are dealt with in the body of the report. But the obligations of non-professional people who make use of the securities market are no less onerous. I do not myself believe that a statutory system, however well organised, would in general operate so efficiently. In this country the two systems of voluntary regulation and of statutory inquiries should be complementary to each other.

Indeed, in one particular field, that of "insider trading", statutory powers are–as The Stock Exchange and the Panel have for several years pointed out–necessary. I would not, however, wish to exaggerate the extent of the evil here. The Stock Exchange is in these times of economic uncertainty and lack of confidence extremely volatile, so that market prices may be affected by matters which on reflection are seen to have little real significance.

There has, however, been too much speculative movement based on rumours of company changes and The Stock Exchange and Panel have, as the body of this report indicates, concerned themselves with this aspect of the matter. These are, as experience has elsewhere shown, matters which cannot be avoided simply by the enactment of statutory regulations: the important thing is the disclosure of full and accurate information at the earliest possible moment.

But just as the voluntary system may no doubt continue to be improved, as is in fact happening, so also the statutory machinery under the Companies Acts can, without undue bureaucratisation, be made more efficient. It is at present open to serious criticism under various heads. Thus the reasons why in a particular case an Inspectorate is set up or, on the contrary, is not appointed, are not always obvious even after the event. There are sometimes inevitable delays in bringing an inquiry once established to its conclusion (the inquiry into the Pergamon affair was only concluded eight years after its commencement). The appointment of unsuitable persons as Inspectors and the occasional tendency of such persons to exceed their powers and give expression to *obiter dicta* outside their legitimate terms of reference but without any right of appeal are possibly inherent risks.

It must also, however, be remarked that many matters which the media invariably headline as “Another City scandal” have nothing to do with the securities industry and are, therefore, outside the jurisdiction of either the Panel or the Council of The Stock Exchange. Some of these matters might fall under the scope of the Companies Acts, but occasionally are not made the subject of inquiry. The Panel and The Stock Exchange are sometimes blamed for failing to investigate cases of alleged misconduct by, for instance, directors of public companies. But they have no jurisdiction so to do except in the context of The Stock Exchange Regulations and the City Code within the operation of the securities industry. Fortunately, such cases of supposed misconduct are certainly not more frequent in the City than in professional and other activities not associated with the City at all. The City of London remains, in spite of all the economic vicissitudes to which the United Kingdom has been subjected, one of the two leading financial centres of the world and certainly second to none in the reputation which it deservedly enjoys for integrity and efficiency. It will, I know, adapt its regulatory arrangements to whatever is required in order to maintain this so far unchallengeable position.

This is an occasion of hail–and farewell. The year has seen changes in the Panel executive in that Mr. Martin Harris, the Director General, and some members of the

staff, the period of their secondment to the Panel having expired, have moved on and Mr. David Macdonald, formerly Chairman of the City Working Party and a most experienced merchant banker, has with several others joined the executive. To the former the sincere thanks of the City are to be recorded. To the latter a warm welcome is extended in the sure knowledge that they will maintain and promote the high reputation which the Panel enjoys.

8th September, 1977.

REPORT ON THE YEAR ENDED 31st MARCH, 1977

STATISTICS

Activity in the take-over field increased during the year ended March, 1977. The Panel was convened three times to hear appeals by parties to take-over transactions against rulings by the executive and three times to consider disciplinary cases brought by the Director General. The Panel met on a further occasion to consider a matter referred by the Director General. There were no cases before the Appeal Committee during the year.

The statistics and commentary on them given below cover transactions where there was at least a public announcement of a firm intention to make an offer.

There were 199 (*148*) take-over or merger proposals of which 189 (*139*) reached the stage where formal documents were sent to shareholders. These proposals were in respect of 188 (*145*) target companies of which 170 (*130*) were listed on The Stock Exchange. In 11 (*3*) cases there were rival offers. 4 (*2*) opposed offers succeeded; no (*1*) agreed offers failed.

A further 38 (*28*) cases which were still open at 31st March, 1977 are not included in these figures. The executive was consulted in another 117 (*87*) cases which either did not lead to published proposals or were transactions, involving control blocks of shares, approved by shareholders.

Category of documents	1976/77	*1975/76*
Circulated by Exempted Dealers … … …	123	*85*
Circulated by Licensed Dealers … … …	9	*10*
Circulated by others exempted under the Prevention of Fraud (Investments) Act, 1958 … … …	27	*17*
Circulated on the basis of specific authority from the Department of Trade … … … …	11	*6*
Scheme of Arrangement … … … …	19	*21*
	189	*139*

Outcome of the proposals	1976/77	*1975/76*
Successful proposals involving control (including Schemes of Arrangement) … … … …	138	*117*
Unsuccessful proposals involving control … …	27	*8*
Proposals withdrawn before issue of documents (including offers overtaken by higher offers) … …	10	*9*
Offers and Schemes of Arrangement involving minorities … … … … …	24	*14*
	199	*148*

INVESTIGATIONS INTO DEALINGS: ANNOUNCEMENT OF PRICE-SENSITIVE MATTERS

Lack of care about security, loose talk, the observation from outside of unusual activity at a company's offices, speculative hunches and dealings by insiders are just a few of the causes of sharp rises in the market price of securities before the announcement of price-sensitive matters. For years The Stock Exchange and the Panel have been carrying out exhaustive and costly investigations into such cases to find out whether there have been breaches of the Rules covering secrecy, the proper timing of the dissemination of information to shareholders or insider trading. The major objectives are to prevent small shareholders from parting with their shares just before the shares become especially valuable and to stop unethical practices.

That there are great difficulties is indisputable and these have been experienced in all countries where sophisticated stock market systems exist. The view of The Stock Exchange and the Panel that true insider trading should be the subject of legislation is well known and the Government's recent confirmation that insider dealing legislation will be introduced as soon as opportunity permits, is warmly welcomed.

There are other things that can be done in a move for further protection of the small shareholder, and, as a reminder about the need for secrecy during negotiations, The Stock Exchange and the Panel issued new guidelines in April: a copy of the joint statement is included as an appendix to this report. In the light of this statement additions and changes will in due course be made to Practice Note No. 9 in respect of Rules 5 and 7.

Perhaps the major innovation in this joint initiative has been to encourage companies to apply to The Stock Exchange for a temporary trading halt. This is a particularly appropriate step when an announcement of importance is imminent but full details are not available, perhaps because certain formalities remain to be settled. In the 5 months since the joint announcement was issued 30 companies have applied for a trading halt in the context of a merger or take-over proposal. This is an encouraging development and it has generally been noticeable that there have been fewer cases of speculative activity in the shares of companies which subsequently announced merger or take-over plans.

OTHER PANEL INVESTIGATIONS

In the discharge of its duty to ensure that those who are actively engaged in take-over or merger transactions in the United Kingdom shall conduct themselves in accordance with the provisions of the City Code, the Panel may investigate *ex post facto* the conduct of the parties or of the advisers who may be assisting them. These enquiries are usually started by the Director General on his own initiative although the exercise of that initiative may be the result of a complaint from one of the parties involved in the transaction or from a member of the public.

In the context of an alleged breach of the provisions of the Code which call for the disclosure of full and accurate information, the Panel considers it to be of general interest to explain the nature of its investigations and the significance of any conclusions reached. It is particularly relevant to describe the position taken by the Panel where parties may contemplate litigation in relation to some aspect or consequence of the merger or take-over.

The Code is designed essentially to ensure that through the adoption of good business practices in the conduct of take-overs and mergers, the confidence of actual and potential investors in the United Kingdom securities market is maintained and enhanced. As indicated in the introduction to the current edition of the City Code, it represents the collective opinion of those professionally concerned in this field as to a range of business standards. A Panel investigation of this sort is intended primarily to ascertain whether the conduct of the parties concerned has measured up to the general standards set by the Code and, in particular, whether or not shareholders have been given full and accurate information. It will be important to ascertain whether there has been proper compliance with the provisions of Rule 14, relating to the standards of care with regard to statements contained in any document or advertisement addressed to shareholders in connection with an offer, and with Rule 15, concerning the duty to put shareholders in possession of all the facts necessary for the formation of an informed

judgment as to the merits or demerits of an offer. Whilst the Panel may conclude that some form of censure should be made or remedial action required, it is not normally a principal object of the investigation to provide remedies for those who consider themselves aggrieved.

The Code does not constitute a detailed directive on practices and procedures for the conduct of directors and professional advisers in the discharge of their obligations under the Code. It is for them to decide in the light of the circumstances of each case, what steps must be taken to comply with the spirit as well as the letter of the Code, and to meet the high standards which have come to be expected from those involved. The Panel is therefore reluctant to embark upon a detailed analysis of the practices and procedures adopted; nevertheless when it is clear that the expected standards of conduct have not been maintained the Panel will not hesitate to criticise the parties concerned.

When the Panel has completed its investigation it may decide that there is nothing in the conduct of the parties which merits taking action in public. In coming to such a conclusion it may consider that whilst certain conduct may not be beyond criticism, nevertheless public criticism could be too severe a penalty. In that event, although no public statement would be made, the Panel might well comment privately to the parties on their conduct.

The Panel would normally consider it inappropriate to pursue an investigation into the conduct of the parties to a take-over or merger at a time when that conduct is the subject of legal proceedings which have already been set in train. It is clear that any publication of Panel findings could well prejudice the outcome of the litigation. In such circumstances, the Panel will usually delay the commencement of its own investigation until the outcome of litigation is known.

The absence of a Panel statement cannot be used as evidence that the conduct of the parties is thought to be beyond reproach since either views may have been expressed privately or the Panel may have reserved its position pending the outcome of litigation.

INDEPENDENT ADVICE FOR SHAREHOLDERS

Rule 4 of the Code requires the board of an offeree company to obtain competent independent advice on any offer and that the substance of such advice be made known to its shareholders. This requirement is of importance in any offer, but it is of particular importance in cases where the controlling shareholder is making an offer to the outstanding minority holders. In such cases the responsibility borne by the independent adviser is considerable and, because of this, it is essential that his independence from the parties involved should be beyond question.

The Code does not require the board of an offeror company to seek independent advice on a proposed offer. There have been a few cases in recent years where, because of the unusual circumstances, for instance cross-shareholdings between the companies and a number of directors common to both companies with shareholdings in each company, it has seemed in retrospect that the interests of the offeror company's shareholders would have been better served if independent advice on the offer had been given to them. In these circumstances the offeror company will usually need to hold a general meeting, so shareholders as a body have an opportunity to consider any advice given and in the light of that advice to authorise or reject the proposed offer.

The Panel recommends that, in those fairly rare cases where there is an apparent conflict of interest between companies, their boards or their large shareholders, the board of the offeror company should give serious consideration to obtaining independent advice on the offer and making the substance of that advice known to its shareholders. The Panel makes a similar recommendation where the offer being made is a reverse take-over, a transaction usually taken to mean one in which, if the offeree company were to become a wholly owned subsidiary of the offeror, the offeror would need to issue more than 100 per cent. of its present issued capital.

OBLIGATIONS OF A FINANCIAL ADVISER

It is a well established feature of the way in which the Code operates that the Panel is entitled to expect the utmost candour and full disclosure from those who are involved in its work and appear before it. This general obligation applies with special force to those who are actively engaged in the securities market in the United Kingdom. They are represented on the City Working Party and the Take-over Panel and are pledged to support both the Code and the Panel by their associations. The Panel has considered the question of what should be a financial adviser's duty to the Panel, during the course of a Panel enquiry, when he has reason to doubt the accuracy or completeness of information being given to the Panel. When a financial adviser finds himself in such a difficult position and is faced with a situation where he thinks the Panel is being misled, the Panel considers that his overriding duty is to the Panel. If, despite his advice, he believes that his client intends to pursue a course of conduct misleading to the Panel, he may ultimately decide to resign. If he does resign, the Panel considers that he then has no obligation to inform them of his misgivings about the conduct which his former client is intending to pursue.

The CBI, as the member of the Panel most closely representative of the corporate clients of financial advisers, has confirmed that it supports the need for full disclosure and accepts that the financial adviser should not be expected to shield a client who was endeavouring to mislead the Panel during an investigation.

AMENDMENT TO RULE 31 OF THE CODE

In broad terms, section 26 of the Companies Act 1976, which came into effect in the middle of April, has led to the public disclosure of dealings in securities where the holder has, or comes to have, over 5 per cent. of the voting rights of the relevant class of shares. In sympathy with this change, Rule 31 of the Code has been amended to require that during an offer period where a disclosure will be required under the Companies Act then such disclosure should be made to The Stock Exchange, the Panel and the press not later than 12 noon on the dealing day following the date of the relevant transaction.

The detailed disclosure requirements, which arise through the inclusion in the Code's definition of associates, for a person or group holding 10 per cent. or more of the equity share capital of an offeror or offeree company are unchanged.

An amendment slip covering the new wording of Rule 31 is enclosed with this report.

INTERNATIONAL DEVELOPMENTS

The Panel remains closely concerned with the proposed securities legislation and take-over and merger control within the EEC. The preliminary draft Directive on take-overs which was considered during 1975 and 1976 by an EEC Working Party which the Panel assisted, has proceeded no further during the year under review. The Panel has also, together with other interested parties, advised the Department of Trade on the United Kingdom's attitude to the draft Directive relating to mergers between companies within individual member states. Similarly, the Panel has been consulted during the drafting of a Code of Conduct which takes the form of a Recommendation from the Commission (not having the force of community law) relating to transactions in the securities markets in the Community. This Code, which draws upon the United Kingdom experience, was formally adopted in July 1977 and will be published shortly.

Contacts have been maintained with regulatory authorities in the major financial centres of the world and in particular visits have been made to the Securities and Exchange Commission in the United States.

The international study group, of which Mr. T. P. Lee of the Panel executive is a member, met in London this summer. The group, drawn from eight countries, was given a full and detailed account of how the securities market is regulated in this country. A number of City bodies and individuals greatly contributed to the success of the week.

(*Addition to Rule 31*)

Furthermore, dealings by any person, who is not an associate, in the shares of an offeror or the offeree company during an offer period which would have to be notified to the company by reason of Section 26 of the Companies Act 1976 and Section 33 of the Companies Act 1967 must be disclosed to The Stock Exchange, the Panel and the press not later than 12 noon on the dealing day following the date of the relevant transaction. The disclosure must name the person dealing and the resultant holding.

8th September, 1977

PRACTICE NOTE NO. 9: PUBLICATION OF RULINGS OF GENERAL INTEREST

In the past the Panel's annual reports have sometimes included an appendix giving rulings of general interest made during the year: subsequently items appearing in these appendices have been embodied in Practice Notes. To simplify looking up references, the Panel had intended in future to publicise such rulings by amending the general loose leaf Practice Note No. 9 and issuing a new version of it with the annual report in each year that it is necessary to make changes.

This year the Panel had expected to issue a new version of Practice Note No. 9 at this time, which would have included, *inter alia*, a detailed interpretation concerning Rule 23 and shut-off notices of alternative offers following the Panel's public statement of 27th May. It has taken longer than expected to reach agreement on one aspect of this, namely how cash underwritten alternatives should be dealt with in a competitive situation. It has therefore been decided to delay the release of the Practice Note until this point has been resolved.

In the meantime the Panel considers it would be helpful to give the following guidance in respect of Rules 22 and 23. In general the provisions of these Rules apply equally to alternative forms of consideration. However, where an alternative offer is cash provided principally by third party underwriting, a statement in the offer document limiting the availability of the alternative to the approximate period of the arrangements with the underwriters on which is it based, will be considered to be a satisfactory notice for the purpose of Rule 23 (1). Thereafter, provided the offeror has not used additional embellishment calculated to persuade offeree company shareholders that the alternative will not in any event be renewed, the offeror will be permitted to procure an extension of the original or a new alternative offer.

STAFF

Since the last annual report Mr. M. R. Harris has been succeeded by Mr. D. C. Macdonald of Hill Samuel & Co. Limited as Director General. Mr. C. R. Ward returned to Whinney Murray & Co. at the end of June and has been replaced by Mr. R. A. Wade of Coopers & Lybrand.

APPENDIX

JOINT STATEMENT ISSUED BY THE STOCK EXCHANGE AND THE PANEL ON TAKE-OVERS AND MERGERS ON 14th APRIL, 1977

ANNOUNCEMENT OF PRICE-SENSITIVE MATTERS

When negotiations are in progress or arrangements are being discussed concerning price-sensitive matters, it has recently all too frequently been the case that the eventual announcement has been preceded by rumours and by an abnormal level of speculative activity in the shares concerned with a corresponding effect on the market price. This has happened most noticeably in the case of merger and take-over announcements. The Stock Exchange and, where appropriate, the Panel have conducted exhaustive investigations into dealings in many cases when a substantial market price movement has been observed in the course of The Stock Exchange's normal monitoring procedures and this movement has assumed a special significance in the light of the subsequent announcement. In almost every instance it has been found that where dealings have taken place they have been carried out by persons who are not insiders but who have acted on what turns out to be a well founded tip or rumour. Only very rarely does it appear that insiders have dealt either directly or indirectly.

The common feature which has emerged from a number of these investigations is that, whereas security in the early stages has been well observed, there being perhaps only the Chairman of the company or companies involved with one or two close colleagues and representatives from the financial advisers, there comes a stage when this is not so, usually when a wider circle of persons is consulted. These may include senior executives, other advisers and selected shareholders: there have also been cases when talks have been held with trading partners, customers, suppliers and creditors.

It appears that on these occasions an error of judgement has been made in delaying an announcement to a point where knowledge of plans is in the hands of a wide circle of people and where it has become impossible to maintain the necessary degree of security.

The Panel and The Stock Exchange are extremely perturbed at this state of affairs, which tends to attract criticism to those concerned and leads to the presumption that transactions have been carried out by insiders.

Attention is drawn to the following points:–

1. Security and Secrecy

The Panel and The Stock Exchange recommend that practitioners and companies should, where this has not already been done, establish security procedures in regard to price-sensitive matters and that such procedures should be drawn regularly to the attention of those concerned.

It should be an invariable routine for practitioners, at the very beginning of discussions, to advise clients of the importance of these matters. In the case of take-overs, attention should be drawn to the relevant parts of the Take-over Code, in particular to Rules 7 and 30.

2. Listing Agreement

Under Section 4(g) of the Listing Agreement, companies are under an obligation to disclose to The Stock Exchange "any . . . information necessary to enable the shareholders and the public to appraise the position of the company and to avoid the establishment of a false market in its securities". Whereas it is impossible to generalise about the timing of an announcement, since each situation in practice is slightly different, the board of a company must, at a time when developments are on hand which are likely to have a significant effect on the share price, pay strict regard to the position of its shareholders. The lack of a warning announcement in some situations may lead to the establishment of a false market.

3. Timing of Merger and Take-over Announcements

It is not the wish of the Panel or The Stock Exchange to discourage talks on mergers and take-overs taking place between senior members of the management and their advisers and essential regulatory authorities and, wherever possible, being concluded in a confidential atmosphere. Nevertheless the Panel's experience shows that there comes a stage in most take-over negotiations when, with the best security arrangements possible, it is still very difficult to avoid gossip and speculation developing. Because of this, and with the intention of achieving a greater degree of adherence to the provisions of Rule 5 of the Take-over Code, the Panel will, in future, normally expect an announcement to be made in the following circumstances:–

(a) where negotiations have reached a point at which a company is reasonably confident that an offer will be made for its shares; or

(b) where negotiations or discussions are about to be extended to embrace more than a small group of people. An obvious example is the case where consultation with more than a very restricted number of shareholders will be involved.

A potential offeror should not take steps to prohibit an offeree company making an announcement under Rule 5 at any time it considers appropriate.

4. Temporary Halt in Dealings

It is appreciated that, even though an announcement may be called for, in some circumstances this can be difficult. Where for special reasons a short delay in making an announcement is necessary, it may be appropriate to request The Stock Exchange to grant a temporary halt in dealings. Temporary halts have become more common in recent years; they are increasingly considered to be a much better course for a company to adopt than to risk the sometimes very damaging sharp movement in its share price caused by partially informed speculation.

Rule 5 of the Code includes a requirement that during negotiations a close watch should be kept on the market and in the event of any untoward movement in the share price an appropriate announcement should immediately be made. As indicated, The Stock Exchange itself monitors price movements very closely and many announcements by companies have been made following approaches by The Stock Exchange as a result of this surveillance. Where there is a significant price movement and no satisfactory explanation or denial of knowledge is forthcoming from the company, The Stock Exchange will itself consider halting dealings temporarily.

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