The Panel on Take-overs and Mergers

Report on the Year ended 31st March, 1987

MEMBERSHIP OF THE PANEL

Robert Alexander QC (Chairman)	Nominated by the Governor of the Bank of England
J. F. C. Hull (Deputy Chairman)	Nominated by the Governor of the Bank of England
Sir Philip Shelbourne (Deputy Chairman)	Nominated by the Governor of the Bank of England
Sir Austin Pearce	Nominated by the Governor of the Bank of England
The Hon. T. J. Manners	Nominated by the Accepting Houses Committee
P. R. Dugdale	Chairman, Association of British Insurers
T. G. Abell	Chairman, Association of Investment Trust Companies
The Rt. Hon. The Lord Boardman	Chairman, Committee of London and Scottish Bankers
M. G. Taylor	Nominated by the Confederation of British Industry
M. V. St. Giles	Chairman, Financial Intermediaries, Managers and Brokers Regulatory Association
A. Green	President, Institute of Chartered Accountants in England and Wales
The Hon. Sir Henry Fisher	Chairman, Investment Management Regulatory Organisation
The Lord Rockley	Chairman, Issuing Houses Association
J. J. McLachlan	Vice-Chairman, National Association of Pension Funds
A. McL. B. Large	Chairman, The Securities Association
Sir Nicholas Goodison	Chairman, The Stock Exchange
W R. Stuttaford	Chairman, Unit Trust Association
The Rt. Hon. The Lord Roskill	Chairman of the Appeal Committee of the Panel

THE PANEL EXECUTIVE

J. L. Walker-Haworth	Director General
P. R. Frazer T. P. Lee	Deputy Directors General
A. D. Paul P. D. Kennerley	Secretaries
N. P Hinton	Deputy Secretary
D. A. J. McKechnie C. C. T. Pender Miss B. A. Muston Miss S. M. Govier R. J. Hilton B. C. K. Timbrell S. A. Atkinson A. M. Keir Mrs. J. M. Taylor Mrs. T. A. Scott	Assistant Secretaries

CHAIRMAN'S STATEMENT

I write this statement after only a few weeks as Chairman of the Panel. I would like at the outset to pay tribute to my predecessor, Sir Jasper Hollom, and to his Deputy, Robin Stormonth-Darling, and to thank them for their very considerable service to the Panel.

It has been a dramatic year in the City of London. We have witnessed very considerable changes in the operation of the stock market, and also in the development of the regulatory system within which the market operates. There have also been highly publicised cases which have created understandable concern as to how regulation can be improved so as to ensure that the reputation for integrity which is essential to the continuing success of the financial markets is maintained. That success, as the growth in the volume and value of transactions indicates, is still striking. We must protect the basis of both skill and fair dealing on which it has to be founded.

The work of the Take-over Panel is one aspect of market regulation. Our role must be seen in the context of the new regulatory structure which is to govern the workings of the financial services industry. The Financial Services Act embodies a statutory framework which recognises the concept of self-regulation. The Panel is a prime example of self-regulation, or rather regulation by the consensus of its members, in action. We co-operate, however, in our work closely with other regulatory bodies and, as I shall mention later, will do so even more effectively when the rules of the Securities and Investments Board ("SIB") and the new self-regulating organisations ("SROs") come into operation.

In accepting the post of Chairman, I was influenced by my belief that institutions and professions should be required to play a leading part in their own regulation. My own profession, the Bar, is a self-regulating profession. This places on its members the responsibility for ensuring standards of discipline, ethics, qualification, and competence. In regard to the City of London, I would echo a recent comment by Sir Nicholas Goodison:

> "There is no financial system in the world which does not depend to a large extent on the moral standards and disciplines of self-regulation."

In what is so far a very short experience, I have seen in action a number of advantages which the Panel gains from self-regulation. It is worth reminding ourselves of them.

Because it operates a non-statutory Code, the Panel is able to do more than enforce simply the minimum standards which could be achieved through legislation. It can base its rules on concepts of best practice, which reflect evolving standards and can be developed as new situations give rise to novel issues. This flexibility also enables

the Panel to stress the importance of compliance with the general principles of the Code and not merely with specific rules. If we had a legislative system, the rules would either have to be less strict, so giving less protection to shareholders, or they would be wide-ranging as at present but without the ability to mitigate their potential harshness in appropriate cases. Moreover, a statutory system could lead to some practitioners seeking to design ways around the strict rules in preference to complying with the principles. Such an approach would not promote good business practices. It is, moreover, only if there is flexibility that the Panel is able in some individual cases to apply the Code in a way which is consistent with the principles of fairness which underlie the Code.

I am aware that some would say that the price of flexibility is a lack of certainty. This is not so; the Panel offers and encourages consultation ahead of action. In this way rulings can be given which enable a bid to proceed without breaches of the Code and with certainty established in regard to conduct during the bid. In saying this, I stress the importance of consulting the Panel ahead of action wherever doubt arises; it is not a substitute for a party to consult its own lawyer or other adviser.

A second major advantage of self-regulation is the involvement of practitioners on the Panel. The Panel is able to count on the commitment and practical support of those who are actively involved in take-overs, whether as advisers, shareholders or management. It is of great help in deciding what is required as a matter of best practice that the rules are formulated with the substantial involvement of practitioners. In the same way, the involvement of practitioners of quality with a direct concern for the fair conduct of take-overs greatly strengthens the decisions of the full Panel. In my short time on the Panel, I have already come to appreciate the depth of experience and dedication which its members bring to our work. In addition, as a self-regulating body, we are able to attract to the Panel executive practitioners and professionals of high ability on secondment from a variety of organisations who blend their own skills and experience with those of the permanent members of the staff.

A third strength of the system, which owes a good deal to the flexibility of self-regulation, is the speed of the service offered by both the executive and the full Panel. This is absolutely essential where rulings are being sought in the course of take-overs. I do not believe it could necessarily be maintained under a statutory regime, and I do not think the excellent record of the executive and full Panel in working so speedily should make us take this aspect of the Panel's contribution during take-overs in any way for granted. It can only be preserved by an informal system and the co-operation of those involved. Speed of service is crucial. The full Panel is greatly assisted by practitioners making written submissions in advance, and by the good sense and economy of oral presentation. We shall, in all cases which call for detailed reasons, seek to give them so that those involved and the public may understand the basis of our decisions.

I am also impressed by the way in which, with self-regulation, we are able to ensure fairness in areas going well beyond the requirements of disclosure and avoidance of misrepresentation which other jurisdictions largely tend to focus upon. Let me give two examples of this approach. First, the Panel works on the basic principle that equality of treatment for shareholders is of the essence of fairness. It follows that when control of a company passes all shareholders must share in the premium for control. This the Code achieves in the ordinary way by requiring a mandatory offer to be made where there is a change in control (which is taken as passing at a level of 30%). All shareholders are then offered the highest price paid by the new controller (and those acting in concert with him) within the previous year. Secondly, the Panel adopts the principle that a board of an offeree company may not take action which could result in a bona fide offer being frustrated or in the shareholders being denied an opportunity to decide on its merits. The Code, therefore, requires an offeree board to seek shareholder approval for issues of shares, material acquisitions and disposals and for contracts otherwise than in the ordinary course of business. Too strict an application of this rule would place unacceptable restrictions on the proper role of the company's management. So the rule has to recognise there are circumstances, whether by reason of the size of the transaction, or the stage of negotiations which has already been reached, when the management must be allowed to go ahead with its plans. In this area the Panel thus has to balance on the one hand the need to ensure that an offer is not frustrated, and, on the other hand, the proper exercise of the management's functions. It is vital to apply the rule according to the spirit as well as the letter.

The work of the Panel has not only increased in recent years, but it has also become of interest to a wider shareholding public. We shall seek to bear this in mind in the course of our work, and, wherever possible, will try to be available to explain what we do both in articles and in response to enquiries from the media. Limitations must, of course, continue where we are dealing with situations on a confidential basis.

We are also concerned that companies, as well as their advisers, should be involved in consultations which affect them. We welcome the fact that a representative of the company concerned normally appears at a full Panel hearing. We would also encourage attendance of representatives of the companies involved at meetings which their advisers may seek with the Panel executive. It is in the nature of our work that some may disagree from time to time with our conclusions, but we do wish to reach them on a fully informed basis and to explain why we have done so.

It is sometimes said that the Panel lacks adequate power of sanction. In fact, the decisions of the Panel are in practice complied with. Almost all of those with whom the Panel deals are concerned to comply, and to be seen to comply, with the Code. This reflects in very great part the grave damage to the reputation of individuals,

advisers and companies which would result from a breach of the Code or a failure to accept our decisions. Support for the Panel in the future has been increased following the announcement in May of the outcome of the review which was carried out by the Department of Trade and Industry ("DTI"), the Bank of England, the Treasury, The Stock Exchange, SIB and the Panel. The review recognised the importance of co-operation between regulators, and the Panel is now authorised to receive restricted information obtained through the use of statutory powers. SIB and relevant SROs are to require practitioners to co-operate with Panel investigations and this will be backed up where necessary by the use of the DTI's own far-reaching investigative powers. In addition, the sanctions of SIB and SROs are to be available for use against practitioners if breaches of the Code are such as to show them not to be "fit and proper" to carry out their businesses, and SIB and SROs are to adopt "cold shoulder" rules, requiring investment businesses not to act for persons who they have reason to believe would not comply with UK practice and standards in take-overs.

This reappraisal of the Panel was of immense value. The review tackled areas of co-operation and inter-action between the Panel and other regulatory authorities and firmly established the Panel's position in the new statutory framework. The Panel has now emerged strengthened to meet the challenge facing all regulatory bodies. It can draw upon the considerable powers of the new structure. It should not be forgotten that events which have given rise to disquiet over the last year took place before the new disclosure rules and stock market monitoring machinery were in place following Big Bang and before the new regulatory system was established.

This leads me to some of the individual developments over the year.

Surveillance

Since Big Bang, sophisticated equipment has been available to the Surveillance Division of The Stock Exchange, giving rapid access to full Stock Exchange dealing data. The Panel, working closely with The Stock Exchange, is therefore now able to monitor dealings in relevant securities during an offer. In this way it is able to identify substantial dealing activity, or unusual price movements, with a view to detecting possible breaches of the Code and cases of market manipulation through lack of disclosure. This is a great step forward from the means of monitoring transactions available in the past.

Multi-service financial organisations

Big Bang led to the establishment of multi-service financial organisations arising from, for example, the acquisition by banks of firms of stockbrokers and jobbers.

The Panel had to address the question of the extent to which part of such an organisation could deal as principal, whether as market-maker or otherwise, in securities of companies involved in a take-over, when some other part of the organisation was acting as financial adviser to one of those companies. Similar considerations arose when part of an organisation was managing funds on a discretionary basis; the question was the extent to which dealings in securities relevant to a take-over effected by the fund manager on behalf of its clients should have Code consequences. In general, the Panel's approach was to allow exempt market-makers and fund managers to continue their operations during the course of an offer, broadly without Code consequences, provided it could be established that those operations were being run wholly independently and, in particular, without regard to the interests of clients of the corporate finance arm. A corollary of that approach was that dealings by those persons should be subject to disclosure to ensure that the Panel and others interested in the take-over could be satisfied that those operations were, in practice, being conducted independently. Major amendments were therefore introduced to the Code in October 1986 to meet these requirements in preparation for Big Bang.

Wider disclosure of dealings

An example of the Panel's ability to reflect best practice, and change rules speedily, is its approach to dealings in shares during an offer. The Panel promotes the important principle, embodied in the Code, that all parties to a take-over transaction must use every endeavour to prevent the creation of a false market. Those who have a special interest in the outcome of an offer may be dealing, or inducing others to deal or to refrain from dealing, for their own purposes. These actions can mislead or distort the market. The Code has therefore for some time required prompt and detailed disclosure of dealings not only by associates but also by those with significant shareholdings. Until recently this meant that, during take-overs, those who had 5 per cent. shareholdings disclosable under the Companies Act had to disclose dealings by the following day. In January it became apparent that, in a take-over context, the 5 per cent. level was too high. Undisclosed dealings below that level could still influence the market. The Panel decided that a level of 1 per cent. was more appropriate. Moreover, shareholdings must not be dispersed between connected parties to avoid disclosures or hidden behind nominees; holdings of connected parties or nominees have to be disclosed in such a way that the real controller can be identified. Although the existing companies legislation went some way to meet these concerns, by their very nature statutory rules are complex and susceptible to evasion if interpreted strictly; moreover, to require groups holding 1 per cent. in total, using the existing wide Companies Act definition, to disclose dealings by the following day would at present be unworkable. Rules for disclosure need to be drawn widely but applied flexibly. The Panel, therefore, taking advantage of its ability to act swiftly to meet changing circumstances and practices,

introduced its own new rule requiring disclosure of dealings by shareholders owning or controlling 1 per cent. of a company involved in a take-over.

Duties of Directors

In July this year the Panel published its statement on the involvement of the full board of a company in an offer. The Panel had been considering the implications of situations in which responsibility for the day-to-day conduct of offers was left in the hands of a small number of directors. Each director has a responsibility under the Code to ensure, so far as he is able, that the Code is complied with. While boards may delegate the day-to-day conduct of an offer to individual directors or committees, the board as a whole must ensure that proper arrangements are in place to monitor that conduct. The relevant directors or committee should promptly provide the board with copies of all documents and announcements issued by or on behalf of their company; report to the board details of all dealings in relevant securities, and details of any non-routine agreements, understandings or expenditure; and should be in a position to justify to the board all courses of action. When relevant, the opinions of professional advisers should be available to the full board. Any director who may have a question concerning the propriety of any action as regards the Code should ensure that the Panel is consulted. Financial advisers have a special responsibility to ensure that all directors are aware of their responsibilities under the Code. The Panel expects directors to co-operate with the Panel in its enquiries. I believe that this approach should go a considerable way towards ensuring an awareness on the part of all directors of actions taken during an offer. This will, in turn, focus a greater degree of accountability to their fellow directors on those who have the day-to-day responsibility for the conduct of the offer.

Judicial Review

Last year, the Court of Appeal held that decisions of the Panel were subject to judicial review by the Court. However, the Court of Appeal recognised that, given the special nature of the Panel and its functions, the market in which it operates and the timescales which are inherent in that market, speed and certainty of Panel decisions are of great importance. The effect of the judgment should mean that the Panel's decisions are treated as valid and binding until they are set aside by the Courts and so applications for review should not be used as a tactic in the course of an offer. The guidelines laid down by the Court of Appeal should ensure that the possibility of an application for judicial review will not inhibit the workings of the Panel and its executive.

Membership

Two new SROs, the Investment Management Regulatory Organisation and The Securities Association have joined the Panel. Mr. John Hull and Sir Philip Shelbourne have agreed to serve as Deputy Chairmen and Sir Austin Pearce as a further independent member. Lord Roskill has been appointed Chairman of the Appeal Committee.

I have highlighted only some of the general matters affecting the Panel during the past year. The level of take-over activity has remained high. During the year the Panel supervised or monitored 280 published take-overs. Whilst we are constantly looking for ways to improve both our service and our effectiveness, I believe that the way in which the Panel does its work makes a substantial contribution to the maintenance of orderly behaviour and fair dealing in the market. I would like to express the great appreciation of the Panel to our executive for their continued skill and dedication.

23rd September, 1987

REPORT ON THE YEAR ENDED 31st MARCH, 1987

STATISTICS

During the year the Panel held 9 meetings to hear appeals by parties to take-over transactions against rulings by the executive and 5 to consider matters referred by the executive. One of the appeals was allowed. There were 3 appeals, each arising from the same case, heard by the Appeal Committee during the year; none was allowed. In addition to its regular quarterly meetings, the Panel held special meetings to consider amendments to the Code; first to deal, in the post Big Bang era, with the position of multi-service financial organisations generally and, in particular, market-makers, and secondly to alter the disclosure of dealings requirements during offer periods and to establish a new system of monitoring of dealings, jointly with The Stock Exchange.

There were 280 *(year ended 31st March, 1986 — 206)* published take-over or merger proposals of which 275 *(197)* reached the stage where formal documents were sent to shareholders. These proposals were in respect of 265 *(195)* target companies, of which 231 *(168)* were listed on The Stock Exchange; 1 *(1)* involved an offer for a private company of the kind subject to the Code. In 15 *(11)* cases there were one or more rival offers. There were 5 *(6)* offers carried out by means of Schemes of Arrangement.

A further 37 *(42)* cases, which were still open at 31st March, 1987, are not included in these figures. The executive was engaged in detailed consultations in another 153 *(167)* cases which either did not lead to published proposals or were transactions, subject to approval by shareholders, involving controlling blocks of shares.

Outcome of proposals	1986/87	*1985/86*
Successful proposals involving control (including Schemes of Arrangement)	211	*138*
Unsuccessful proposals involving control	50	*38*
Proposals withdrawn before issue of documents (including offers overtaken by higher offers) ..	5	*9*
Offers and Schemes of Arrangement involving minorities	14	*21*
	280	*206*

STAFF

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

Mr. P D. Kennerley of Simmons & Simmons has been appointed joint Secretary.

Mr. J. G. Palfrey, Mr. R. A. Randall, Mr. G. Williams and Mr. G. W. Woolley have left the executive. Mr. B. C. K. Timbrell and Mrs. T. A. Scott of the Bank of England, Mr. S. A. Atkinson of Ernst & Whinney and Mr. A. M. Keir of Midland Bank plc have joined the executive.

It has been announced that Mr. A. R. Beevor of Hambros Bank Limited is to be appointed Director General with effect from 11th December, 1987 in the place of Mr. J. L. Walker-Haworth, who will be returning to S. G. Warburg & Co. Ltd.

FINANCE

The Panel is financed by members' contributions, by a levy on certain transactions in United Kingdom securities and through charges in relation to offer documents. Details of the levy and the document charges are set out in the Code.

Expenditure for the year to 31st March, 1987 was as follows:–

	(£000)	
	1987	*1986*
Personnel costs	1,007	*703*
Accommodation costs	387	*216*
Other	427	*256*
	1,821	*1,175*

The increase in personnel and accommodation costs over the previous year reflects an increase in the Panel's staff and a corresponding rearrangement of the Panel's offices.

(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****.)*