The Panel on Take-overs and Mergers

Report on the Year ended 31st March, 1974

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
J. M. Clay	Chairman, Issuing Houses Association
M. Haddon-Grant	Chairman, The National Association of Pension Funds
*D. A. Hunter Johnston	Deputy Chairman, Association of Investment Trust Companies
*G. A. Loveday	Chairman of the Council of The Stock Exchange
*A. Macdonald	Chairman, British Insurance Association
D. H. Maitland	Chairman, Association of Unit Trust Managers
Sir Peter Menzies	Nominated by the Confederation of British Industry
*Sir John Prideaux	Chairman, Committee of London Clearing Bankers
*M. J. Verey	Chairman, Accepting Houses Committee

*Since the last Annual Report Mr. D. A. Hunter Johnston, Mr. G. A. Loveday, Mr. A. Macdonald, Sir John Prideaux and Mr. M. J. Verey have been appointed in place of Mr. A. G. Touche, Sir Martin Wilkinson, Mr. K. M. Bevins, Sir Eric Faulkner and The Viscount Harcourt.

Lord Pearce	Chairman of the Appeal Committee of the Panel

THE PANEL EXECUTIVE

John Hull	Director General
B. J. Denington P. R. Frazer	Deputy Directors General
H. J. Trembath	Secretary
T. P. Lee	
C. M. de Boer	
I. L. Clarke	

FOREWORD

The City Panel has completed a further year of work which, although in some respects less active for reasons explained in the body of this Report, has continued to consolidate the Panel's usefulness and authority.

At a time when existing institutions and arrangements are under attack, often for no better reason than that they are existing and so regarded as part of an "establishment" which should be destroyed, it is right to emphasise the high degree of success which self-regulation and discipline have achieved in this field.

In whatever field of activity, statutory regulations administered by legal authorities can, at the best, lay down no more than minimum standards of behaviour. The danger always is that once such standards are established as rules of law, they come to be regarded as the maximum of what is required and the lawyers (of whom I was one) exercise their ingenuity in finding, as they are entitled to do, ways of avoiding or by-passing the application of the legal rules. Moreover, there is a necessary rigidity in legal rules, a time lag–often very considerable–in adapting them to new circumstances and a tendency to bureaucratisation (if such a word exists) in their administration.

In this country the statute law as enacted by Parliament does of course apply to very many aspects of company activity, including mergers and take-overs. But what is regarded as good ethical practice has in this field gone far ahead of what Parliament has or indeed ever could lay down. It may indeed be said as a general proposition that where the aim is to establish high standards of conduct in technical or professional matters, the only way in which the maximum standards can be obtained is by self-regulation and discipline. Certainly in regard to take-overs and mergers it is the fact not only that many of the abuses which occurred before the formation of the City Panel could not in practice have been avoided by statutory regulation but that since the Panel asserted its discipline they have, for the most part, ceased to exist. And this in spite of the allegation which is often made that the Panel lacks "teeth".

On every working day the Panel executive, in response to enquiries from those concerned in take-over bids or mergers, make some thirty to forty rulings. These rulings are subject to appeal to the Panel but in practice of the several thousands of rulings given at the executive level in each year only a very small number (on average some six or seven) are disputed by the parties affected, and an even smaller number are appealed (as is possible, for example, in disciplinary cases) to the Appeal Committee, after hearing by the Panel. Many of the decisions involve serious financial implications for those affected by them but in no case has the decision of the Panel on an interpretation of the Code been challenged or ignored. It is perhaps a tribute to the generally high standard of behaviour which the City Panel exists to promote that public censure or criticism by the Panel is now regarded as a very grave matter indeed. It would be a brave firm or individual–and also a very foolish one–who defied the Panel's decision.

It should be added that, although the Panel meets infrequently to hear actual appeals, I and my colleagues do of course keep in constant touch with the day-to-day administration and the general trend of rulings being given. The Director General has the right, which he is encouraged to exercise, of referring any case which he considers of particular doubt or difficulty to the Panel for decision without first giving a ruling and throwing the onus of appealing against it on the parties. In this way the Panel is able to ensure flexibility and the quick adaptation of the Panel's practice or the alteration of its rules to meet new or changing circumstances. Here, because the General Principles enunciated in the Code are paramount, our administration has great advantages over one depending entirely on explicit legal regulations. Nothing illustrates this better than the way in which the Code, brought together and revised in what was for most of the time a bull market, has been applied to the different circumstances of the present bear market. Moreover, our administration disposes in hours or, at the most, days of matters which under a legal system would be likely to take months or years.

And does so with great economy in cost. Where the attainment of high ethical standards is the objective, cost should not be a primary consideration. But it is the case that under the very different circumstances and history in the United States which have necessitated the establishment of the Securities and Exchange Commission (with which organisation we have a most agreeable communication) the Commission's own budget last year was over $36 million and its staff nearly 2,000. This is to say nothing of the very heavy professional fees which the Commission's inevitably more litigious procedures necessarily involve. Even so, in the United States, there are many matters which still have to be dealt with by self-regulation.

In our rather peculiar circumstances I am myself convinced that the highest standards will still best be secured by our present "voluntary" system. Where, (as in the case of insider dealing) we feel that we cannot adequately control any particular situation, we shall not hesitate to ask for the provision of statutory remedies.

Compared with its American counterpart, the staff of the Panel executive is surprisingly small. Not surprisingly, in view of their number, the members have to work exceedingly hard, often until late into the night. I should like to record, on behalf of the full Panel, our very warm appreciation of all that they do.

It is appropriate also that I should refer to the impending departure of two members of the executive. Mr. John Hull became Director General of the Panel on 1st April, 1972. The period for which he was kindly seconded to us by Schroders expired earlier in the current year, but Mr. Hull has been good enough to stay on until now in order to ensure a smooth transition to his successor. Mr. Hull now goes back to take up a senior appointment in Schroders. He has, during his term of office, served with untiring energy, enthusiasm and ability and I am sure that I am expressing the view of the City generally in thanking him most warmly for his help.

Mr. Basil Denington was seconded to us by the Council of The Stock Exchange on 3rd July, 1972. Since then, he has acted as Deputy Director General and it is from this position that he is about to retire. I should like to record also, with our gratitude, the help which he has generously given to the Panel throughout that period.

We welcome, in place of Mr. Hull, Mr. Martin Harris, a Senior Partner of Price Waterhouse & Co., who has had a most distinguished career as a Chartered Accountant and who will, I know, bring that distinction to his work with the Panel.

21st October, 1974.

REPORT ON THE YEAR ENDED 31st MARCH, 1974

General

The economic situation and the general decline in the stock market were reflected in a lower level of activity in the field of take-overs and mergers during the year. In spite of the decline in the number of transactions there was a substantial increase over the previous year in the number of cases brought before the Panel and several of these cases involved meetings of the Panel extending over more than one day.

In addition to the routine Quarterly Meetings, 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. A further eight cases were referred to the Panel by the Director General; five of these concerned Rule 8 (new Rule 9) of the Code and the implications for an offeror where there have been changes in economic or other circumstances since the date of the announcement of an offer.

The Appeal Committee met twice under the chairmanship of Lord Pearce. The meetings were held to consider appeals from the Panel's rulings in two of the disciplinary cases referred to above.

Statistics

The Panel executive was concerned with take-over or merger proposals made in respect of 263 companies (last year 353) of which 207 (*260*) were companies whose securities were quoted on The Stock Exchange. In 21 (*31*) cases there were one or more rival offers and altogether there were 286 (*388*) proposals of which 266 (*356*) reached the stage where formal documents were circulated to shareholders. 3 (*3*) agreed offers failed and 1 (*8*) opposed offer succeeded.

These statistics and the information given below cover transactions where there was at least a public announcement of a firm intention to make an offer. A further 26 (*48*) cases still open at 31st March are not included in these figures. The executive was consulted in another 140 cases which either did not lead to public proposals or were transactions approved by shareholders involving control blocks of shares.

Category of documents

	1973/4	*1972/3*
Circulated by Exempted Dealers … … …	189	*248*
Circulated by Licensed Dealers … … …	16	*26*
Circulated by others exempted under the Prevention of Fraud (Investments) Act 1958 … … …	30	*42*
Circulated on the basis of specific authority from the Department of Trade … … … …	10	*25*
Scheme of Arrangement … … … …	21	*15*
	266	*356*

Outcome of the proposals

	1973/4	*1972/3*
Successful proposals involving control (including Schemes of Arrangement) … … … …	163	*214*
Unsuccessful proposals involving control … …	36	*36*
Proposals withdrawn before issue of documents (including offers overtaken by higher offers) … …	20	*32*
Offers and Schemes of Arrangement involving minorities and unconditional offers following the transfer of effective control	67	*106*
	286	*388*

Note**: Cases involving reverse take-overs of public by private companies have been excluded from these figures.**

The Revised Edition of the City Code

A number of cases before the Panel during the year exposed serious difficulties in the interpretation of the rules in the 1972 edition of the Code governing the obligation to make a general unconditional offer when significant holdings of shares are acquired. Accordingly, at the request of the Panel, the City Working Party (the body responsible for the Code) reconsidered and revised these rules and took the opportunity at the same time to make certain further alterations to the Code which experience had shown to be necessary. The Panel has always accepted that the Code will need to be changed from time to time as new situations or techniques arise and it considers that the ability to make such changes with a minimum degree of formality is one of the strengths of the voluntary system. The amended version of the Code was published and came into effect on 6th June, 1974.

The most important amendment (embodied in new Rule 34) has been to require that a general offer should be made when a person (together with persons acting in concert) acquires shares carrying 30 per cent. or more of the voting rights of a company or when such persons, already holding between 30 per cent. and 50 per cent. of the voting rights, increase their percentage of the voting rights by more than 1 per cent. in any period of twelve months. The offer must be in cash and must be conditional on the offeror receiving acceptances, which, together with shares already owned, result in the offeror holding shares carrying over 50 per cent. of the voting rights. No other condition is permitted and no acquisition of shares which might give rise to an obligation to make an offer may be made if the implementation of the offer would depend on any other consent or the making of any other arrangements, e.g. the approval of the offeror shareholders or the completion of underwriting arrangements.

The principal effect of these changes is, first, to eliminate the problems arising under the old rules from the distinction between purchases from selected sellers and general market purchases, and secondly to establish 30 per cent. of the voting rights of a company as effective control for Code purposes in virtually all circumstances.

The new requirement that such an offer should be conditional on the receipt of a minimum level of acceptances has been introduced because the requirement under the old rules that the offer should be unconditional operated against the interests of the majority of shareholders in some circumstances–particularly in cases where there was, or might have been, competition from another bidder.

Necessary consequential changes have been made to the rules dealing with shut-outs, disclosure of shareholdings and *pro rata* partial bids, and, to prevent companies

being under prolonged or permanent siege, a new rule (Rule 35) has been introduced providing that an unsuccessful offeror must not purchase shares during the twelve months following the close of its offer if it would thereby become obliged to make an offer under Rule 34.

There is no doubt that the effect of new Rules 34 and 35 will be far-reaching. Nor is there any doubt that cases will arise where dispensations from the effect of the rules will be necessary in the interests of the shareholders of the offeree company. The new rules are inevitably to some extent experimental and the Panel will not hesitate to suggest further amendments if these are shown to be necessary.

The Code sets out to control actions taken by "persons acting in concert" to the same extent as if such actions were taken by one person or company. This has been, and no doubt will continue to be, an extremely difficult area. An attempt has been made in the Code to specify categories of relationships where there will be a rebuttable presumption that actions taken by any one member of the group are motivated by a common group interest.

In its Report last year the Panel indicated the importance it attached to the requirement of Rule 15 that an offeror must state its intentions with regard to the future of the offeree company. Rule 15 has been extended and amplified and now requires a statement by the offeror in the offer document as to:–

(i) its intentions regarding the continuance of the business of the offeree company;

(ii) its intentions regarding any major changes to be introduced in the business, including any re-deployment of the fixed assets of the offeree;

(iii) the long-term commercial justification for the proposed offer; and

(iv) its intentions with regard to the continued employment of the employees of the offeree company.

Rule 8 has been amended to provide that all conditions to which an offer is subject must be stated in the announcement. Following discussions with the Director General of Fair Trading and the Department of Trade, a specific condition is required in cases falling within the statutory provisions for possible reference to the Monopolies and Mergers Commission that the offer will be withdrawn if the case is referred to the Commission.

Practice Notes and Publication of Rulings

When the new edition of the Code was published in June it was accompanied by a revised Practice Note No. 7, which contains a number of rulings and interpretations of general application. Further such rulings since June are included in Appendix I to this Report.

Ariel

On 11th February the Accepting Houses Computer Share Dealing System–Automated Real-Time Investments Exchange Limited–commenced operations. The executive had discussions with Ariel's management who expressed their wish to co-operate to the full with the Panel in ensuring observance of the Code in relation to transactions effected through their system. In particular, satisfactory arrangements have been made regarding disclosure of dealings and, if necessary, investigations into dealings where it would appear that there has been a leakage of information.

Withdrawal of offers

One of the objectives of the Code is to prevent frivolous and irresponsible announcements of offers and it is for this reason that it provides that an announced offer shall not be withdrawn without the consent of the Panel.

The measures introduced by the Government in the latter part of 1973 to deal with the threatening economic crisis, the collapse of the property market and the three-day week resulted in a number of applications by companies, which had announced offers, for permission to withdraw their offers. In view of the importance of the principles involved, the Panel issued on 15th January and 13th March, 1974 public statements indicating the general considerations which guide its approach to such cases. These statements are re-printed in Appendix II to this Report.

Appeals

The Introduction to the Code provides for a right of appeal to the Appeal Committee in disciplinary cases. The Report of the Panel for the year ended 31st March, 1970 sets out the procedure for an appeal against a disciplinary decision of the Panel and specifies that the party concerned must serve notice of appeal within 48 hours of the communication of the decision to him.

Except in the case of disciplinary matters, there is no absolute right of appeal to the Appeal Committee. The 1970 Report indicates, however, that a right of appeal to the Appeal Committee may also lie, with leave of the Panel, against decisions which, although not strictly of a disciplinary nature, inflict serious hardship on an individual or firm, or when it is alleged that the Panel has acted *ultra vires.* Application for leave to appeal in such circumstances must, as in disciplinary cases, be made to the Panel within 48 hours of the communication of the decision.

European Economic Community

The Panel executive has been visited during the year by certain staff of the European Commission and also by officials of the Commission des Operations de Bourse in Paris. These meetings are welcomed since they provide an opportunity not only to establish direct contacts with the European bodies concerned but also to exchange views on areas of common interest and concern.

A small number of proposed mergers have fallen within the provisions of the Treaty of Paris, which requires prior clearance from the Commission. So far as practicable the Panel treats such a case in the same manner as a merger proposal referred to the Monopolies Commission in the United Kingdom. Accordingly, no offer document should be despatched until the necessary clearance has been obtained and care must be taken in framing the announcement, particularly if the offeror wishes to reserve the right to vary the terms of the offer in the light of circumstances existing when clearance is obtained.

The executive has been represented on various groups set up to consider proposals for future E.E.C. legislation which may have a bearing on the field of take-overs and mergers.

There is currently a debate within the Community as to whether there should now be a move towards harmonisation of take-over and merger procedures within member States. The present view of the Panel is that it would be premature to consider this subject until there has been much further progress towards harmonisation in the field of company law and in the operations of the securities and capital markets within the Community.

Staff

During the year Mr. Peter Frazer, formerly joint Secretary, was appointed a Deputy Director General. Mr. John Trembath joined the Panel on 1st January, 1974 on secondment from Allen & Overy as Secretary in place of Mr. Peter Lee. Mr. Lee left the Panel in December, 1973 on the expiry of his contract period but has since rejoined as special assistant to the Director General. Mr. Christopher Kennedy left on the expiry of his contract period at the end of 1973; his place has been taken by Mr. Christopher de Boer, seconded by James Capel & Co.

APPENDIX I

Rulings and interpretations of general interest.

Rule 11

In cases where the Panel's consent is requested for a sale of shares falling within the provisions of this Rule such consent will only be given on the basis that the directors of the offeree shall not procure the appointment of representatives of the purchaser to the board of the company before the offer document has been posted. When the purchaser is already represented on the board, such representation shall not be increased until after the posting of the offer document.

Rule 34

Where an offeror has elected to include a share alternative in an offer made under this Rule it may not give a shut-off notice under Rule 23 in respect of the cash offer only.

Rule 36

For the purposes of this Rule an arrangement to deal with special favourable conditions attached includes any arrangement whereunder the offeror or potential offeror or a person acting in concert with the offeror promises to make good to a vendor of shares any difference between the sale price and the price of any subsequent successful offer or increased offer.

APPENDIX II

Statement issued by the Panel on Take-overs and Mergers on 15th January, 1974

In view of the present change in the economic and industrial situation of the country and of actual or possible legislation the City Panel has been asked to advise a number of companies on their position under the Code in cases where they had announced an intention to make an offer but had not yet become legally bound by the posting of formal offer documents. The Panel has assisted by giving its view based on the circumstances of each particular case but, at the request of the companies concerned, these opinions have, for good reasons, not been made public. The Panel thinks it may be useful, however, to indicate the general considerations which guide its approach to such cases.

The City Panel will of course give careful consideration to the facts of each particular case which may come before it. In general, however, the Panel considers that a change in economic or industrial conditions, or even in legislative policy, which may suggest that a proposed acquisition will not be as advantageous for the offeror company as was hoped when the intention to offer was first announced, is one of the hazards which has to be accepted in a take-over situation. Even in more normal conditions than now exist, markets are volatile and it must be expected that they will sometimes over a period show wide fluctuations, which may for a time put a different complexion on the economics of a particular offer. On the other hand, falls in market levels or depressions in the general economy are usually followed after a time by recovery. Similarly legislative policy depends upon the exigencies of the time. The City Panel considers that a change in economic, industrial or political circumstances would not normally justify the withdrawal of an announced offer. To justify unilateral withdrawal the Panel would normally require some circumstance of an entirely exceptional nature and amounting to something of the kind which would frustrate a legal contract. It must be remembered that the terms and timing of an announcement of intention to offer and of the posting of offer documents are, subject to the Code, entirely in the hands of the offeror. It is therefore right that an offeror should accept the risk of a change of circumstances in the intervening period. Once an offer is announced, the market in the shares of the offeree company is likely to be, at least to some extent, supported by the price at which the offer has been fixed. It follows that withdrawal would contribute to the market having been a false one.

The Panel has been asked about the position of directors of a company who, having announced an intention to make an offer, become convinced, before a legally

enforceable obligation to offer has arisen, that circumstances have changed so as to make the proposal no longer economically advantageous to their company. Directors are of course trustees for their company in the exercise of their powers. They must always act in good faith; they ought to consider the long term interests of the company and to have regard not only to immediate financial considerations but to the company's public reputation. Thus they should not neglect consideration of the public interest, the regulations of The Stock Exchange (which attach great importance to compliance with the City Code) and the City Code itself, adhered to as it is by the Confederation of British Industry. Consideration of such factors as these have been described as constituting enlightened self-interest on the part of the company concerned, which is expected to behave as a "good citizen". It is not for the Panel, nor even for lawyers, to dictate to directors how they should act in the best interests of their company; this is a matter on which each director must satisfy his own conscience after having regard to all relevant considerations. The Panel can only say that for their part they expect companies to accept the Code as binding upon them; it is well established that the courts will not interfere with directors' exercise of discretionary powers unless it is proved that they have acted from some improper motive or arbitrarily and capriciously. Compliance with the requirements of the City Code voluntarily adopted by the City institutions and by industry in order to promote orderly markets and secure fair treatment for shareholders would certainly not be so considered. The general position is indicated in General Principle 2 of the Code and directors must give due weight to this and the other requirements of the Code.

The general acceptance of the Code, as administered by the Panel, has in more than one case in the past led to the acceptance of some economic disadvantage in the short term. To be offset against this disadvantage is the long term benefit to investors and the financial and industrial community as a whole and to the company in question–as part of that community–which the Code seeks to achieve.

The Panel takes the opportunity of pointing out that Rule 8 of the Code requires the statement in the offer announcement of any conditions to which the offer or the posting of it is subject "other than normal conditions relating to acceptances, quotation and increase of capital". Experience has shown that the omission of the so-called normal conditions can give rise to misunderstanding. The Panel is therefore inviting the City Working Party to consider the deletion of the exception from Rule 8. In the meantime offerors should state all conditions to which their offer is subject without exception and the Rule will be so administered.

Statement issued by the Panel on Take-overs and Mergers on 13th March, 1974

1. One of the objectives of the City Code was to prevent the directors of companies from announcing offers and then without adequate reason withdrawing from them–thus creating a false market and often leading to unfair treatment as between shareholders of the offeree company. The Panel has therefore been and remains very reluctant to agree to the withdrawal of an offer that has been announced. In its statement, dated 15th January, 1974, the Panel indicated that a change in economic, industrial or political circumstances would not normally justify the withdrawal of an announced offer. To justify unilateral withdrawal, the Panel would normally require some circumstance of an entirely exceptional nature, and amounting to something of the kind that would frustrate a legal contract. This statement indicated how existing policy, which regarded the withdrawal of an announced offer as an exceptional matter, was to be interpreted in current circumstances. Directors, in announcing an offer and the terms and conditions on which it will be made, must have carefully considered the matter and must fully intend to go through with the operation.

Conditional Offers

2. Rule 8 of the Code states that the announcement of an offer must indicate any conditions to which the offer is subject and the Panel has recently indicated that this should include, where applicable, what are usually described as the "normal" conditions, viz.,

(i) Percentage acceptance by offeree shareholders (normally 90 per cent. at the outset).

(ii) A resolution of the shareholders of the offeror company.

(iii) Stock Exchange consent to listing of any new capital.

3. Announcements of offers should not include conditions which depend on subjective judgments by directors or the fulfilment of which are in the hands of the directors since these create unnecessary uncertainty; nor should they include a condition that, if the general economic situation deteriorates, the directors can withdraw the offer. It would normally be acceptable in an announcement for an offer to be expressed as being conditional on statements or estimates being appropriately verified.

Monopolies Commission References

4. The Panel believes that in future the best course would be for an offer to be withdrawn on a reference of the proposed merger to the Monopolies and Mergers Commission. This would mean that, in cases of the type that come within the statutory provisions for possible reference to the Commission, the offeror should indicate, as a

condition of the offer, that the offer would be withdrawn if there was a reference. Such withdrawal would not prevent the offer, or another offer, being made if the Monopolies Commission gave the merger a clearance.

Shareholders' Approval

5. There remains the question of the position of directors and shareholders where a resolution of the shareholders of the offeror company is required, e.g., for an increase in authorised capital or under the Regulations of The Stock Exchange.

6. A refusal by offeror shareholders to pass any necessary resolution should not be equated with a withdrawal by directors of an offer. The condition of shareholders' approval would have been specified at the outset.

7. The Panel does not take the view that directors are obliged by the Code to recommend shareholders to vote in favour of such a resolution in all circumstances. Equally, the directors are not free to ignore what they have done in the name of the company. The failure to proceed with an announced offer, even an offer subject to conditions, is a serious matter and the directors must bear this in mind in their recommendation to shareholders. The Panel will not criticise a board that has weighed up, and is seen to have weighed up, all factors in its recommendation. The shareholders are free to take their decision in the light of all the circumstances.

8. The position is different where a company has already incurred under the Code a mandatory obligation to make an offer because of large purchases of shares. Most of these cases involve a cash offer and it is exceptional for the consent of shareholders to be required. Obviously, directors should not incur an obligation to make an unconditional offer under the Code unless they are in a position to honour the obligation. In the highly exceptional case where the approval of shareholders is required, directors have to give their advice to shareholders in the knowledge that a refusal by shareholders to pass the necessary resolution will give rise to a breach of the Code and will result in some penalty or sanction, depending on the circumstances, being imposed on the company in breach.

Announcement of offers

9. In view of the above the Panel stresses the serious responsibility that lies on directors at the time of making an announcement of an offer.

(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.**)