LAW PUNDITS

CROSS BORDER MERGERS REGULATION IN EU

Course Material

Cross border merger regulations in EU

The European regime governing mergers between companies in different member states of the EEA derives from Directive 2005/56/EC, the Directive on Cross-Border Mergers of Limited Liability Companies (Directive).

The UK implemented the Directive via The Companies (Cross-Border Mergers) Regulations 2007, SI 2007/2974, as amended by SI 2008/583 and SI 2011/1606 (Regulations).

The basic framework involves circulation of all relevant proposals to shareholders, approval of the merger by shareholders and creditors, approval of the pre-merger requirements by the court or other competent authority in each member state, approval of the merger by the court in the member state where the merger will be registered, and registration of the merger with the relevant Registrar.

If employee participation arrangements exist in any member state, these will need to be agreed in accordance with Part 4 of the Regulations

Types of merger

The Regulations cover a wide range of restructurings involving a UK public or private company (or an unlimited or unregistered company) merging with one or more companies in another EEA state. Thus the types of merger that may arise can include:

1. merger by absorption, where one or more transferor companies are liquidated and all assets and liabilities transferred to a transferee company.

2. a cross border absorption of an existing wholly-owned subsidiary by its parent, and

3. merger by the dissolution of two or more existing companies with transfer of assets and liabilities into a new company formed for the purposes of the merger

The Takeover Code

In the UK, the City Code on Takeovers and Mergers (Code) will apply in the normal way to the extent that at least one of the companies involved in the merger is covered by the scope of the Code.

The Takeover Panel (Panel) has published a practice statement providing guidance on the application of the Code to cross border merger situations.

A merger by absorption will be subject to the Code if a transferor (ie offeree) company falls into paragraph 3(a)(i) or (ii) of the Introduction to the Code. However even if the offeror

company is a 'Code company', the Code will not apply if the offeree is not a Code company.
Mergers into a newly formed company will be similarly be covered by the Code if one of the transferor entities is a Code company.

Mergers by absorption of a wholly-owned subsidiary are not covered by the Code.

Pre-merger requirements

Before the court will approve the merger, it must have issued a certificate under regulation 6 that all the pre-merger requirements under regulations 7-10 and 12-15 have been complied with.

These requirements are as follows:

1. a draft of the proposed terms of the merger prepared by the directors of the company, with particular information on the share exchange ratio, and the procedures by which employee participation rights are to be agreed

2. a directors' report setting out the effect of the merger on shareholders, creditors, debenture holders and employees, to be delivered to the employees at least 2 months before the meeting to approve the merger

3. in most cases, a report by an independent expert (namely a statutory auditor under the Companies Act 2006) which comments on the share exchange ratio, and details of any third party valuations

4. all documents to be available for inspection at the registered office for at least one month before the meeting to approve the merger. An application can then be made to the court to convene the approval meeting under regulation 11

5. delivery of details of the meeting and other information required by regulation 12 to the Registrar not less than 2 months before the date of the approval meeting, and particular of each merging company on form CB01; and

6. the merger to be approved by a majority in number representing 75% in value, of each class of members, present and voting in person or by proxy (with similar provisions in relation to creditors under regulation 14)

Once the requirements above have been certified in accordance with regulation 6, the court may make an order approving the merger where the offeror (transferee) is a UK company, and all the equivalent procedures have been complied with in each EEA state.

Application must be made to court within 6 months of the pre-merger certificate being granted, and the merger must take place within 21 days of the order approving the merger.

The assets and liabilities of the transferor companies are then transferred to the transferee, and the transferor companies are dissolved. Also, within 7 days of the court

order, all UK companies must file the court order with the Registrar, and in the case of an EEA company transferor, particulars of the register in which it is entered and its registration number.

Employee participation

Cross border mergers must take account of any employee participation arrangements in any relevant EEA state. Such statutory rights to participate at board level do not exist in the UK but do in countries such as Germany, Austria and Spain. Participation can mean a number of things but primarily covers the ability of employees or their representatives to appoint, or recommend or oppose the appointment of, members of the company's administrative forum (or board). The principle of employee participation is that the company resulting from the merger will be subject to the employee participation rules in force, if any, in the EEA state where it will have its registered office.

The participation rights relevant under the UK Regulations are where the transferee company is a UK company and any merging entity has, in the 6 months before the publication of the draft terms of the merger, an average minimum of 500 employees and a system of employee participation, or where a merging company has employee representation on its board or administrative forum.

As soon as possible after adopting the draft terms of merger, each merging company shall provide information to the employee representatives of that company or, if no such representatives exist, the employees themselves.

The merging companies can then agree to be subject to the standard rules on employee participation or alternatively set up a special negotiating body (SNB) as specified under the Regulations.

Employees of merging companies shall be given an entitlement to elect one member of the SNB for each 10% or fraction thereof which employees of merging companies represent of the total workforce of the merging companies, subject to further provisions which give each merging company the right to have at least one constituent member on the SNB.

The merger cannot be completed until all employee participation arrangements have been settled, which can in practice delay the merger by many months.

The employee representatives of the UK transferee company, or if there are no such representatives, the employees, shall have the right to elect, appoint, recommend or oppose the appointment of a number of directors of the transferee company, such number to be equal to the number in the merging company which had the highest proportion of directors (or their EEA equivalent) so elected or appointed.

Every director of the transferee company who has been elected, appointed or recommended by the employee representatives or the employees, shall be a full director with the same rights and obligations as the directors representing shareholders, including the right to vote.

Future developments

In December 2012 the European Commission published an Action Plan (COM(2012) 740/2) in relation to European company law and corporate governance. One aspect of this is to progress the conclusions of a study on the application of the Directive, namely to decide whether to enhance the procedural rules for cross border mergers. The Commission notes at paragraph 4.2 that:

"…there seems to be a particular case for enhancing the procedural rules, given that a number of issues have been identified as a potential source of uncertainty and complexity, in particular a lack of harmonisation as regards methods for valuation of assets, the duration of the protection period for creditors' rights, and the consequences for creditors' rights on completion of the merger."

And further that:

"…the Commission will consider an initiative to provide a framework for cross-border divisions, possibly though an amendment of the cross border mergers Directive, as the latter is well known to stakeholders and it provides a tested framework for cross-border restructurings."