Key Takeaways

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On 8 May 2017, Skadden and Erskine Chambers hosted a comparative corporate law event in conjunction with New York University School of Law and the *Financial Times* entitled "The Great Debate: U.S. v. U.K. — Which System of Takeover Regulation Is Better?" at The Ritz in London. An audience of more than 100 guests gathered to hear a debate on the relative merits of the U.K. and U.S. systems for regulating public takeovers, which was followed by critiques from a distinguished panel.

Skadden partner Michael Hatchard and Erskine Chambers' head Michael Todd QC argued in support of the U.K. system of regulating public M&A transactions. Wachtell, Lipton, Rosen & Katz partner David Katz and Saïd Business School Professor Colin Mayer presented arguments in support of the U.S. approach. The post-debate review panel comprised Delaware Supreme Court Chief Justice Leo Strine, Jr., Vice-President of the Court of Appeal of England and Wales (Civil Division) The Right Hon. Lady Justice Gloster and Deputy Director General of the Takeover Panel Tony Pullinger. Alan Livsey of the *Financial Times* moderated the debate.

The debate required advocates on both sides to give preliminary arguments as to why the takeover regulatory system was superior in either the U.S. or the U.K., and to present rebuttals and closings in turn. The participants covered topics such as the fairness and effectiveness of the regulatory framework, as well as the responsibilities, duties and rights of boards and shareholders in public M&A transactions in the two jurisdictions. The panellists then reviewed the arguments, offered personal insight and inquiries, and answered questions from the audience.

Arguments for the UK

Structure of the UK Regulatory System

Mr. Hatchard and Mr. Todd submitted that the paradigm of any system for the regulation of takeovers is one that:

1. ensures shareholders of an offeree company are afforded equal and fair treatment by the offeror and are not denied the opportunity to determine the merits of the offer; and
2. promotes the integrity of the market.

Mr. Todd explained that the purpose of such a system is to provide an environment within which shareholders may make a fully informed investment decision on the merits (or otherwise) of an offer. He said that it is only right that shareholders — the owners of the company whose economic interests are on the line — decide what is best for the company, not the board.

Legal Framework

The U.K. structure provides just such a system, which Mr. Hatchard suggested is no surprise, given that it has been designed by, and adapted at the instigation of, market participants and the investment community. The City Code on Takeovers and Mergers (the Code) is the bedrock of the system, promoting the key principles of "equality of treatment of shareholders" and "let the shareholders decide". The Panel on Takeovers and Mergers (comprised of an experienced and highly accessible executive) promotes market integrity and confidence in the system by requiring compliance with the Code, through its power to take disciplinary action against participants acting in breach of the rules. Yet, the efficiency of the checks and balances within this Code-enforcement structure ensures that appeals to the Panel are few and far between and appeals to the courts are rarer still.

Mr. Todd also explained the facilitative and informational role played by the board, noting that its members' duties do not extend beyond providing information to shareholders to enable them to make an informed investment decision and, to the extent there are different classes of shareholders, acting fairly as between them. Consistent with the common law, the Code specifically restricts actions by the board that could frustrate an offer.

The US System — an Unworthy Comparator

Mr. Hatchard also remarked that the order and structure inherent in the U.K. system is in stark contrast to the management-driven process in the U.S., where duties to the market are arguably less regulated, targets may be in play for extended periods of time, and shareholders are left with no choice but to litigate when their rights are abused. Mr. Hatchard also critiqued the heavy reliance that U.S. stockholders must place on the target board, which can be inherently conflicted in its motives in response to any offer.

Mr. Hatchard and Mr. Todd concluded by asking the panel and the audience whether investors should be free to decide the future of their investments (as the U.K. structure dictates) or whether that role should be delegated to the board (as is the case in the U.S.). They said the choice must lie with investors, rather than a potentially conflicted board; and outcome which is facilitated by the U.K. regulatory system.

Arguments for the US

Mr. Mayer set the tone for the U.S.'s opening arguments by positing that the U.K. system is too rigid and blindly prioritises minority shareholder protection at the expense of value maximization, product and capital market considerations, and incentives for shareholders to be engaged. Because the U.K. Code protects minority shareholders, there is little incentive in the U.K. to be a majority investor, Mayer argued, which necessarily promotes short-term interests. Mayer also suggested that another unfortunate consequence of the U.K.'s system's "obsession" with minority protection is that investors become spectators rather than players.

Contrasting US and UK Transactions

Both Mr. Mayer and Mr. Katz cited the Airgas/Air Products and Allergan transactions as practical examples to illustrate the key differences between the U.S. and U.K. approaches. The U.S. approach recognises that, while the interests of shareholders are to be respected, not every takeover bid at a premium is in the long-term interests of shareholders or other stakeholders — Mr. Mayer noted that in the U.K., Cadbury was unable to proffer a defence to arbitrageurs selling their shares to Kraft, whereas in *Airgas*, the Delaware courts ruled defensive measures, such as a staggered board, can be properly used by the board to delay or frustrate a deal viewed as "grossly inadequate" and unreflective of a company's long-term value. Mr. Katz referenced the value maximizing success in the Airgas and Allergan cases, as board intervention led the companies to be sold several years later for higher premiums.

Shareholders Have the Final Say

Mr. Katz also articulated the benefits of the U.S. system in allowing directors to consider the interests of all stakeholders in saying no to a takeover bid — not just shareholders. Yet, from the moment that a decision has been made to sell the company, shareholder interests do come to the fore through the obligation on directors to achieve the best value reasonably available.

Mr. Mayer and Mr. Katz closed the arguments for the U.S. by pinpointing why the U.S. regime is superior to the regulatory system in the U.K. The U.K. system, they argued, allows opportunistic bidders to take over companies even if the value offered does not reflect the long-term value of the target, whereas the U.S. approach permits board intervention to achieve long-term value maximisation.

A short period of rebuttals then followed.

Closing Statements

The U.K. team closed by emphasising that the U.K. system treats all shareholders alike, without taking their power away. The advocates reminded the audience that the U.K. has a transparent system, where bidders must disclose interest and purpose. They compared this candidness to a cycle of "misleading impressions" in the U.S. that they referred to as "anarchy". The U.K. "flexibility", they said, is a much better route for the takeover regulatory regime.

The U.S. team, in turn, reminded the audience that the U.S. system is well-regulated with disclosure obligations designed to protect shareholders. While the U.K. has undermined the health of the corporate sector through its regulatory system, the U.S. has permitted directors to run the takeover process in a manner that balances the interests of shareholders and the company. "The board knows best", they say.

Post-Debate Panel Review

The panellists shared their impressions of the debate and discussed the relative merits of the U.S. and U.K. takeover regulatory systems. The Right Hon. Lady Justice Gloster challenged the U.K. side's argument that the Code system in the U.K. is transparent and preferable to litigation in the U.S. She noted that we take for granted that the Panel is acting only for "good" and that perhaps more judicial review is necessary, given our ignorance as to what goes on when the Panel convenes behind closed doors.

Mr. Pullinger endorsed many of the arguments presented by the U.K. advocates and noted the U.K. system's admirable principles of equality and transparency. He contrasted this to the U.S. system, where parties do not always keep their word. Mr. Pullinger questioned the U.S. advocates' reliance on the Airgas example and noted that this is but one example of a successful defensive strategy. He proceeded to challenge the assertion that the board knows better than shareholders, and noted it is simply not the case that the Panel is rigid and inflexible in its approach to monitoring takeovers — the Panel has full discretion to grant dispensations and does so on a daily basis. It also keeps the Code under constant review to ensure that new tactics are appropriately handled.

Chief Justice Strine, however, pointed out that one drawback of the U.K. Panel is that members of its panel are not necessarily versed in corporate law, which is in stark contrast to the Delaware courts. He admitted that there may be too much litigation in the U.S., but suggested that in the U.K. there is too little. He highlighted that the U.K. system fails to maximize value in several ways, one of which is through the obligation to give due diligence rights to all potential bidders and thereby inhibiting the flow of information in practice. The U.S. system, on the other hand, requires boards to defend their actions in the name of shareholders. He referred to the U.S. takeover regulatory system as a Republican Democracy, noting that the board can go against the "electorate" but are still accountable and liable to shareholders.

Key Takeaways

At this year's Transatlantic Comparative Corporate Law event, the arguments put forward by the U.K. and U.S. teams, together with the panellists' perspectives, showed that the U.S. and U.K. systems have commonalities, but are unique in their own ways:

- In both systems, shareholders have the final say on whether to approve a transaction, and the interests of minority shareholders are protected (albeit to different degrees).
- In the U.K., the role of the board in a takeover scenario is limited to ensuring equality of treatment and information and affording shareholders an opportunity to consider every potential offer, whereas in the U.S., the board has the ability to shield shareholders from certain deals, provided it is not acting in self-interest but rather in accordance with its duty to maximize long-term value.
- The U.K. has a more structured takeover process regulated by the Code and the Panel, which results in few takeover disputes coming before the courts. In the U.S., shareholders must litigate to protect their rights.

Associate Claire Cahoon assisted in the preparation of these takeaways.

For additional background, please click here to read Chief Justice Strine's article "The Soviet Constitution Problem in Comparative Corporate Law: Testing the Proposition that European Corporate Law is More Stockholder Focused than U.S. Corporate Law".