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An Evaluation of the EU Takeover Directive (Thirteenth Directive) Through the Lens of the Harmonization Process

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Abstract

This paper examines the implications of harmonization on the EU Takeover Directive (Thirteenth Directive). Ironically, the desire to achieve harmonization of corporate law in the EU is what hinders the Directive's strength and scope. A close reading of the Directive reveals the difficulty of gathering consensus from Member States, as derogations are peppered throughout its provisions. Data on the Directive's implementation does not paint a better picture. The Directive has failed to spur major changes across Member States, and this performance is likely an extension of its weak drafting. The paper then takes on a comparative lens, evaluating differences between the EU and U.S. with regard to their approaches to takeovers. While the intentions of the Directive are pro-shareholder, U.S. corporate law tends to defer to boards of directors, and the latter may be an approach that creates a more robust market for corporate control. Because the Takeover Directive could benefit from both substantive and structural changes, this paper touches upon ways the Directive could take into account the benefits of allowing for takeovers, as well as ways it could become more far-reaching and achieve better implementation among Member States.

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I. INTRODUCTION

The Thirteenth EU Company Law Directive,[1] also known as the Takeover Directive or Takeover Bids Directive, intended to establish a regulatory framework that would create consistency among EU Member States' takeover laws and, by doing so, "create favorable conditions for the emergence of a European market for corporate control."[2] In adopting this Directive, which aims to facilitate takeovers, the EU demonstrated its subscription to the efficient market theory[3]: it views the market for corporate control as a threat to corporations' management that pressures them to perform well and subsequently produces a net social gain.[4] The Directive tries to reset the power balance between corporations' shareholders and boards of directors to restore investors' confidence in the European capital markets as a mechanism of discipline for company management.[5]

II. THE IMPLICATIONS OF HARMONIZATION

While the two goals of the Directive—harmonization and, broadly, shareholder protection—appear to align, attempting to achieve harmonization of corporate law in the EU caps the Directive's ability to really redefine shareholder protection. Harmonization limits the strength and scope of the Directive's provisions and "hinder[s] progress towards a European cross-border M&A [mergers & acquisitions] market,"[6] which would translate into a more robust market for corporate control. Integration unfortunately involves "establishing detailed

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[1] Directive 2004/25/EC of the European Parliament and of the Council of 21 April 2004 on takeover bids, 2004 O.J. (L 142) 12.

[2] Caterina Moschieri & Jose Manuel Campa, *New Trends in Mergers and Acquisitions: Idiosyncrasies of the European Market*, J. BUS. RESEARCH 1, 2 (2013), *available at* http://dx.doi.org/10.1016/j.jbusres.2013.07.018.

[3] Tyler Theobald, *Hostile Takeovers and Hostile Defenses: A Comparative Look at U.S. Board Deference and the European Effort at Harmonization* 33 (Oct. 16, 2006), *available at* http://law.bepress.com/expresso/eps/1838/.

[4] Alexander White, *Reassessing the Rationales for the Takoever Bids Directive's Board Neutrality Rule*, 5 EUROPEAN BUS. L. REV. 789, 792 (2012).

[5] Joseph A. McCahery & Erik P. M. Vermeulen, *Does the Takeover Bids Directive Need Revision?* 3 (Tilburg Law and Economics Center, Discussion Paper No. 006, 2010), *available at* http://ssrn.com/abstract=1547861.

[6] Moschieri & Campa, *supra* note 2, at 2.

substantial rules applying uniformly to all Member States," meaning that rules have to be agreeable to all twenty-eight Member States and flexible enough to accommodate their varying preferences. The Directive format therefore is restrictive. Because of the need to provide Member States sufficient freedom, directives "[do] not dictate the means for achieving [the] result[s]" outlined but rather delegate to Member States the authority to implement rules in their own fashion.

Moreover, as implied by the impracticability of gathering consensus from all Member States, harmonization is "subject to considerable institutional and national barriers."[7] The result of this pushback is that Member States can often derogate from rules, and these exceptions demote many directives to a "semi-success"[8] at best. The Thirteenth Directive unsurprisingly contributes to this pattern of derogation. Although the substance of the Directive's Articles is strikingly powerful, the provisions unfortunately are either optional or riddled with ambiguity that dilutes their strength. The optionality of some of the Directive's most far-reaching sections enables Member States to continue their national practices and retain their takeover systems, consequently doing little to establish an integrated cross-border M&A market throughout the EU. For example, in the case that companies of Member States that adopt such provisions encounter outside-EU bidders or bidders not subject to the same rules, the companies can exempt themselves from the rules.[9] With such features tempering much of the Directive's language, it seems more accurate to call the Directive's "rules" a set of guidelines for Member States.

The history behind the development of this Directive illustrates that the concessions on the shareholder-protection front indeed were made in an attempt to integrate. Discussions about a possible takeover directive for the EU began fourteen years before the European Parliament

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[7] *Id.*
[8] Magnier, *supra* note 6, at 107.
[9] *Id.*

reached an agreement,[10] and early versions of the legislative product caused political controversy among Member States. Many did not welcome European-wide regulation of takeovers, understandably so since there is great variation among the Member States.[11] Numerous political compromises therefore were made throughout the negotiation and drafting process to get everyone on board and to satisfy various interest groups (e.g., large corporations and firms, which benefit from defensive practices, have powerful interest groups that worked to block harmonization efforts[12]), which left a "significantly diluted" version of the European Commission's original proposal for the Directive.[13] The Council finally approved the Directive on April 21, 2004. It was published in the *Official Journal of the European Union* on April 30, 2004, and entered into force on May, 20, 2004.[14]

Commissioner Balkenstein commented that he did not consider the Directive "a step forward for EU competitiveness or for the integration of EU capital markets," and he regarded the belief that the resulting text would establish a level playing field of takeover regulation across Member States a "delusion."[15] Nonetheless, some consider the Directive to be "a significant legislative accomplishment, worthy of attention [in part] . . . for its contribution to the ongoing debate over the desirability of harmonization versus regulatory competition."[16] And even though the Directive may not carry as much force as initially expected, it does establish a baseline for takeover regulation and provides at least some harmonization of takeover bids

[10] Slaughter and May, *The European Takeovers Directive – an Overview*, SLAUGHTER AND MAY 3 (Sept. 2006), https://www.slaughterandmay.com/media/39335/the_european_takeovers_directive_-_an%20overview.pdf.
[11] Marco Ventoruzzo, *Europe's Thirteenth Directive and U.S. Takeover Regulation: Regulatory Means and Political and Economic Ends*, 41 TEX. INT'L L.J. 171, 174 (2006).
[12] McCahery & Vermeulen, *supra* note 5, at 6.
[13] Slaughter and May, *supra* note 10, at 3.
[14] *Id.*
[15] *Id.* (internal quotation omitted).
[16] Ventoruzzo, *supra* note 11, at 174.

processes given that Member States now have a common framework for reference when discussing or changing takeover regulations.

III. THE THREE RULES OF THE THIRTEENTH DIRECTIVE

The tension presented by the Directive's intention to harmonize helps explain the Directive's provisions, which frequently appear to conflict with or work against one another. The Directive has three main components: the mandatory bid, board neutrality, and breakthrough rules.[17] These rules primarily regulate the bid process and target boards' use of defensive tactics.

A. Mandatory Bid Rule

The first rule is derived from Article 5(1) of the Directive, which requires controlling shareholders to make a bid for the corporation at an equitable price, whether the controlling ownership in the corporation's securities is acquired alone or in concert with others.[18] The purpose of this provision is to give minority shareholders a "unilateral exit right"[19] that enables them to leave the corporation by tendering at a fair price. Yet the rule is vague in several areas. For example, "control" is undefined, so it is unclear what threshold of ownership triggers a compulsory bid; Member States are left to determine such details.[20]

Although it is easy to quickly frame the discretion given to Member States as a concession made in exchange for harmonization, upon further evaluation, such deference may be preferable. National legislatures may be best positioned to adopt appropriate definitions and thresholds for their markets given that what is appropriate for each Member State is largely determined by its economic characteristics. For instance, "a 30 percent threshold [could]

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[17] *Id.* at 206.
[18] Directive 2004/25/EC, art. 5.
[19] Edmund-Philipp Schuster, *The Mandatory Bid Rule: Efficient, After All?*, 76 MOD. L. REV. 529, 533 (2013) (quoting P. L. Davies, 'The Notion of Equality in Corporate Takeovers' in J. Payne (ed), Takeovers in English and German Law (Oxford: Hart Publishing, 2002) 12-13).
[20] Ventoruzzo, *supra* note 11, at 206 (citing Directive 2004/25/EC, art. 5).

significantly raise the cost of hostile takeovers in a system with very concentrated ownership" where most companies have controlling shareholders, but such a threshold could be "significantly less relevant in a system where control can be easily acquired [by] obtaining a lower percentage of shares."[21] Therefore, rather than attempting a one-size-fits-all approach—whether that be assuming that the mandatory bid rule applies whenever an acquirer obtains *de facto* control over a corporation[22] or relying on 30 percent as the threshold for control[23]—, variation among States' definition of the rule's trigger may be necessary to produce a consistent outcome throughout the EU.

The mandatory bid rule also regulates the price of any compulsory bids arising from Article 5(1). According to Article 5(4), "equitable price" is defined as the highest price paid for the corporation's securities by the controlling shareholder over a period of between six to twelve months before the bid; Member States choose the exact duration of such time period.[24] The price of the compulsory bid therefore "includes the entire premium for control,"[25] and while favorable toward minority shareholders, this demand could deter value-maximizing hostile takeovers from occurring since a bidder buying control would have to offer the same price to minority shareholders as well.[26] Any premium paid to the controlling shareholder would essentially be shared with all other shareholders.[27] Since the bidder is forced to treat all shareholders equally, the pricing requirement is often called the "equal opportunity rule"[28] and embodies the idea that a control premium is the *corporation's* asset, not the controlling shareholder's.[29]

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[21] *Id.* at 207.
[22] Schuster, *supra* note 19, at 532.
[23] *Id.*
[24] Directive 2004/25/EC, art. 5.
[25] Ventoruzzo, *supra* note 11, at 207.
[26] *Id.*
[27] Schuster, *supra* note 19, at 532.
[28] *Id.*
[29] *Id.* at 536.

The aforementioned provision seems potentially ineffective because in its attempt to protect minority shareholders, it could chill the market for corporate control and undermine one of the Directive's main goals. Because bidders are required to "offer to all shareholders [] a pre-share price equal to the consideration received by the incumbent controller, an otherwise profitable transaction might lose its economic rationale for the bidder,"[30] given that acquisitions will become more expensive for bidders. At issue is "whether the aggregate value of the non-value maximizing transactions that [the rule] deters is greater than the aggregate value of the efficient takeovers that would have occurred in its absence."[31]

Perhaps because of such concerns, in what becomes a noticeable pattern throughout this Directive, the rule is tempered. Article 5(4) allows Member States' supervisory authorities to adjust this price "in circumstances and in accordance with criteria that are clearly determined."[32] Although Member States cannot adopt provisions generally allowing compulsory bids to be launched at prices lower than by the standard laid out in the Directive, the provision enables States to adjust price by creating a "relatively extensive list of circumstances" that serve as exceptions.[33] This language gives Member States the freedom to change rules to limit the extent to which minority shareholders can share control premiums.

B. Board Neutrality Rule

The second rule of the Directive, the board neutrality rule, is modeled after the UK's City Code on Takeovers and Mergers and addresses post-bid defenses.[34] Article 9(2) prohibits directors of target corporations (i.e., corporations facing hostile bids) from taking actions that

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[30] *Id.* at 533.
[31] McCahery & Vermeulen, *supra* note 5, at 9.
[32] Directive 2004/25/EC, art. 5(4).
[33] Ventoruzzo, *supra* note 11, at 208 (citing Directive 2004/25/EC, art. 5(4)).
[34] Guido Ferrarini & Geoffrey P. Miller, *A Simple Theory of Takeover Regulation in the United States and Europe*, 42 CORNELL INT'L L.J. 301, 313 (2009).

frustrate bids, such as adopting poison pills, without receiving prior shareholder approval to do so.[35] Moreover, it requires target boards to "publish a statement of its evaluation of the offer and its possible effects, including its effects on employment levels and on the relocation of company activities."[36] This rule does not affect board decisions that are "part of the normal course of the company's business,"[37] though, and because it is unclear how to distinguish a corporation's "normal course of business" from that which is not, target boards could try to frame some defensive tactics so that they appear to fall outside the rule's scope.

Target boards need not play this interpretation game, however, because the seemingly powerful board neutrality rule is optional.[38] Even if Member States opt into the rule, they can choose to condition its application on reciprocity[39]; in other words, corporations of opted-in Member States can "disapply the rule if they are subject to a bid by a company from a jurisdiction which does not impose it."[40] But corporations can also individually voluntarily opt into the rule with a supermajority vote of their shareholders even if their Member State has opted out,[41] and such allowance secures shareholders the opportunity to have some say in how their board responds to bids. Member States cannot prevent corporations from voluntarily applying the board neutrality rule, for it simply needs to be adopted at a general meeting.[42]

If Member States opt into the rule, their target boards are required not only to consider all acquisition proposals, but also to consider stakeholders of the company aside from shareholders when evaluating proposals. This approach thus integrates both board- and shareholder-centric

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[35] *See also* Ventoruzzo, *supra* note 11, at 208 (citing Directive 2004/25/EC art. 9(2)).
[36] Directive 2004/25/EC art. 9(5).
[37] *Id.* at art. 9(3).
[38] *Id.* at art 12(1).
[39] Ventoruzzo, *supra* note 11, at 212.
[40] White, *supra* note 3, at 791. "[R]eciprocating power can be used only if it is authorized by both the Member State and the general meeting of the target company." *Report on the Implementation of the Directive on Takeover Bids*, at 5, SEC (2007), 268 (Feb. 21, 2007).
[41] *Id.*
[42] *Report on Implementation of Directive*, *supra* note 40, at 5.

views of the corporation. By prohibiting the target board from implementing perhaps the most effective takeover defense (i.e., the poison pill) without shareholder approval, the rule gives target shareholders "exclusive decision-making power in [the] takeover bid situation"[43] and ensures that minority shareholders have the chance to tender their shares. The board neutrality rule protects shareholders from possible opportunistic behavior by the board[44] yet simultaneously is considerate of the social entity view of the corporation, which asserts that shareholders, while owners of the company, are not the only group that the board should have in mind when assessing bids.[45] Rather, the board is to take into account various factors like a bid's impact on "the company's interests and specifically employment."[46]

For Member States opting into the rule, neutrality applies "'at least' from the time when information regarding a bidder's intention to launch a tender offer is made public,"[47] until the bid completes or lapses.[48] Member States can extend the reach of the board neutrality rule by setting its trigger as when the target board "becomes aware that the bid is imminent."[49] This is unlikely a popular choice among Member States, though, because altering the trigger in this way would increase the vulnerability of their corporations to foreign bidders.[50]

The board neutrality rule facilitates takeover activity, which the High Level Group of Company Law Experts (HLG)—established by the Commission during the Directive's proposal stages to provide recommendations—views as generally beneficial.[51] According to HLG,

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[43] White, *supra* note 3, at 789.
[44] *Report on Implementation of Directive*, *supra* note 40, at 5.
[45] *See* Lynn A. Stout, *Bad and Not-So-Bad Arguments for Shareholder Primacy*, 75 S. CAL. L. REV. 1189, 1190 (2002) (describing the "entity view" as one that emphasizes interests of not just shareholders, but also stakeholders like employees, creditors, and the community at large).
[46] Directive 2004/25/EC, art. 9(5).
[47] *Id.* at art. 9(2).
[48] Slaughter and May, *supra* note 10, at 6.
[49] Directive 2004/25/EC, art. 9(2).
[50] Ventoruzzo, *supra* note 11, at 209.
[51] White, *supra* note 3, at 790.

takeovers "create wealth by exploiting synergies and [] discipline the management of listed companies with dispersed ownership, which in the long term is in the best interests of all stakeholders, and society at large."[52] The neutrality rule thus abides by efficient market theory in restricting board defenses from barring hostile takeovers[53] and embodies the notion that "[d]efensive mechanisms are often costly," "managers [] face[] [] a significant conflict of interests," and "[s]hareholders should be able to decide."[54] As with the mandatory bid rule, the board neutrality rule advocates shareholder primacy, but to a greater extent since it directly restricts the board's decision-making power (in contrast to the mandatory bid rule, which simply promotes takeover activity by affecting the bid process). This difference may help explain why the board neutrality rule is subject to an opt-out.

C. Breakthrough Rule

The third main component of the Directive, outlined in Article 11, addresses pre-bid defenses in the takeover context by aiming to close loopholes that would remain even if Member States implemented the board neutrality rule. While the board neutrality rule aims to limit target boards' use of defensive strategies, boards can still "adopt certain provisions designed to entrench control, or at least make a successful hostile offer much less likely to succeed[,]"[55] that fall outside the scope of that provision. For example, boards can adopt dual-class shares, shareholders' agreements limiting transferability of shares, and supermajority vote requirements for approving freeze out mergers after the bid.[56] The Directive thus provides the breakthrough

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[52] *Id.* (quoting *Report of the High Level Group of Company Law Experts on Issues Related to Takeover Bids*, at 2 (Jan. 10, 2002), *available at* http://ec.europa.eu/internal_market/company/docs/takeoverbids/2002-01-hlg-report_en.pdf).
[53] *Report on Implementation of Directive*, *supra* note 40, at 5.
[54] White, *supra* note 3, at 790 (quoting *Report of the High Level Group of Company Law Experts on Issues Related to Takeover Bids*, at 2 (Jan. 10, 2002), *available at* http://ec.europa.eu/internal_market/company/docs/takeoverbids/2002-01-hlg-report_en.pdf).
[55] Ventoruzzo, *supra* note 11, at 209.
[56] *Id.* at 210.

rule, which "makes certain restrictions . . . inoperable during the takeover period and allows a successful bidder to easily remove the incumbent board of the target company and modify its articles of association."[57] During the period of an offer, restrictions on share transfers cannot be applied to the bidder; restrictions on voting rights cannot be used to approve frustrating actions; and multiple voting rights and any special arrangements for appointing board members are ignored once a bidder acquires 75% voting ownership of the target corporation.[58] The breakthrough rule neutralizes other defensive devices to (i) deter director entrenchment and prevent target boards from rebuffing economically efficient offers and (ii) establish a level playing field across Member States.[59]

According to Article 11, when a bid is made public,[60] any contractual agreements or corporation bylaws that allow restrictions on securities transfers or the exercise of voting rights are "rendered ineffective until the end of the offer."[61] This rule also authorizes bidders who successfully complete a bid (i.e., tender enough shares) to appoint new directors or amend the charter or bylaw provisions,[62] enabling the corporation's new controlling shareholder to "sterilize [] defenses [from] operat[ing] ex post."[63]

Whereas this rule would effectively expand the market for corporate control, as with the board neutrality rule, the breakthrough rule is optional (although Member States that opt out must let corporations registered in their State opt into the rule via shareholder resolution, and a reciprocity exception is also present here).[64] The harmonization motivations of the Directive offer some rationale for the watering down of the rules. To implement some kind of takeover

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[57] *Report on Implementation of Directive*, *supra* note 40, at 5.
[58] Slaughter and May, *supra* note 10, at 6 (citing Directive 2004/25/EC, art. 11(2)-(4)).
[59] Ventoruzzo, *supra* note 11, at 210.
[60] Directive 2004/25/EC, art. 11(1).
[61] Ventoruzzo, *supra* note 11, at 210.
[62] Directive 2004/25/EC, art. 1(19).
[63] Ventoruzzo, *supra* note 11, at 211.
[64] Slaughter and May, *supra* note 10, at 6 (citing Directive 2004/25/EC, art. 12(1)).

regulation on the European level, it was necessary to compromise with Member States that opposed the more controversial parts of the proposed Directive. While the mandatory bid rule survived the lengthy discussion and proposal process (albeit with enough vagueness for Member States to manipulate to their liking), the latter two components of the Directive did not have such lucky fates. Given their extremity—the board neutrality rule limiting defensive actions by target boards and the breakthrough rule making any other such mechanisms inoperative in the face of a takeover—, perhaps it is not surprising that they faced resistance and were deemed optional. The mandatory bid rule is less dramatic and even resembles some regulations in the U.S.; moreover, before adoption of the Directive, most Member States had a similar requirement present in their legal systems, which diminished opposition to the rule. Even without the Directive, Member States were generally united on this front, meaning that the Directive's work in this area may be redundant.[65]

IV. IMPLEMENTATION OF THE THIRTEENTH DIRECTIVE

The question now is whether the Directive has fulfilled its goal: has it operated as an effective governing mechanism on behalf of minority shareholders that improves the market for corporate control?[66] The answer appears to be no. In 2012, the Commission evaluated the Directive's application and concluded that it "has not led to major changes in the legal framework of [] Member States."[67] For one, the Directive's allowance of derogations[68] obviously diminishes its impact and makes it difficult to predict its influence. As stated by the Commission, the "ultimate impact of the Directive [] depends largely on the modalities of its implementation in the Member States and on the extent to which they will use the exemption[s]

[65] Schuster, *supra* note 19, at 532.
[66] McCahery & Vermeulen, *supra* note 5, at 4.
[67] *Application of Directive 2004/25/EC on Takeover Bids*, at 3, COM (2012) 347 final (June 28, 2012).
[68] *Id.* at 6.

provided for in the Directive."[69] Implementation has involved strong national biases,[70] and the strength of shareholder groups in each Member State also plays a role in Member States' takeover regulations and abidance by the Directive since takeover rules "tend to reflect the interests of respective political power of the bidders and targets in a particular jurisdiction."[71] For instance, if shareholder interest groups are powerful in a given Member State, it will probably abide more closely by the Directive's recommendations since it can identify a greater demand for shareholder protection. There is tentative evidence that differences in Member States' takeover regulations reflect differences in the power balance between targets and bidders among Member States, and protectionism, an unintended effect of the Directive, tends to be greater in Member States where targets have more to fear from hostile takeovers.[72]

The ability to opt out also discourages Member States from participating in much of the Directive's framework. As of June 2012, only three Member States—Latvia, Lithuania, and Estonia—had adopted the breakthrough rule,[73] and these Baltic States chose to make the rule optional for their companies.[74] Furthermore, this rule actually negatively affects many corporations incorporated in Scandinavian countries (Sweden, Norway, Finland, and Denmark) since they tend to have "dual class voting structures with multiple voting shares, which would be 'broken through' [were] the companies [] to adopt" Article 11.[75] Member States therefore seem to be wary of any disproportionate effects of implementing the Directive's rules.

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[69] *Report on Implementation of Directive*, *supra* note 40, at 3.
[70] Moschieri & Campa, *supra* note 2, at 2.
[71] McCahery & Vermeulen, *supra* note 5, at 5.
[72] Ferrarini & Miller, *supra* note 34, at 331.
[73] *Application of Directive on Takeover Bids*, *supra* note 67, at 8.
[74] McCahery & Vermeulen, *supra* note 5, at 5.
[75] Andrew Zwecker, *The EU Takeover Directive: Eight Years Later, Implementation But Still No Harmonization Among Member States on Acceptable Takeover Defenses*, 21 TUL. J. INT'L & COMP. L. 233, 255-56 (2012).

According to a 2010 study, nineteen Member States had opted into the board neutrality rule, yet all but five had such an obligation in place prior to the Directive's adoption.[76] Moreover, given that corporate ownership in the EU tends to be "concentrated in a few shareholders or a shareholder holding enormous blocks of shares,"[77] even in Member States where the rule is in effect, the controlling shareholder will largely decide how defensive tactics are used rather than minority shareholders, the intended recipients of the decision-making power delegated away from the board. It is also notable that five of the fourteen Member States that already had a mandatory bid rule in place opted into the reciprocity exception,[78] which dilutes the rule's impact. This exception has been justified as enabling Member States to give boards greater room against foreign hostile bidders and to maintain a balance between both the target and bidder in the corporate control context,[79] but it may be contributing to a protectionist stance by Member States. In 2007, the Commission confirmed this view by expressing disappointment with Member States for acting in a "seemingly protectionist way"[80] and for apparently using the Directive's exemptions as a means to strengthen the role of target boards in employing defensive tactics against bidders.[81] Commissioner McCreevy has conceded that "the protectionist attitude of a few seems to have had a knock-on effect on others,"[82] and if this attitude becomes a trend, the resulting barriers to takeovers will directly undermine the intentions of the Directive.

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[76] White, *supra* note 4, at 791 (citing Paul L. Davies, Edmund-Philipp Schuster & Emilie Van de Walle de Gheicke, *The Takeover Directive as a Protectionist Tool?* (ECGI – Law Working Paper, No. 141, 2010), *available at* http://ssrn.com/abstract=1554616).
[77] Theobald, *supra* note 3, at 47.
[78] White, *supra* note 4, at 791.
[79] *Report on Implementation of Directive*, *supra* note 40, at 8.
[80] *Id.* at 10.
[81] Magnier, *supra* note 6, at 108.
[82] Blanaid Clarke, *The Takeover Directive: Is a Little Regulation Better Than No Regulation?*, 15 *European Law Journal* 174, 196 (2009) (quoting Press Release, European Commission, IP/07/251 (Feb. 27, 2007), *available at* http://europa.eu/rapid/press-release_IP-07-251_en.htm).

Few Member States have been willing to interfere with corporations' antitakeover arrangements,[83] and most have taken advantage of the opt-out provision to avoid participating. Article 12 lets Member States (i) refuse to adopt the board neutrality and breakthrough rules (though corporations can still individually opt in); (ii) adopt either of the aforementioned rules but condition the rules' application on reciprocity; or (iii) adopt both rules without a reciprocity exception.[84] Member States have little incentive to choose the third alternative, particularly since other Member States do not enforce both rules stringently. The hope seems to have been that even with the board neutrality and breakthrough rules not being mandatory, shareholders would take advantage of the provisions enabling their corporations to opt into the rules even if their Member States had not. But it is unclear whether there is a lot of individual opting in by companies and little data exploring this level of implementation. Moreover, whereas there are legitimate reasons for opt-outs, such as lowering "cost[s] due to corporate governance diversity"[85] and accommodating the large variation in types of firms and cultural environments across the EU,[86] they undeniably weaken integration. Optionality was included in the Directive to cater to all Member States and to enable the Directive to come into fruition, but in hindsight, it has prevented true harmonization from occurring on an implementation level since Member States can simply ignore certain aspects of the Directive.

The Directive has also caused problems for Member States that already had minimum takeover standards in place, like the UK and Ireland.[87] It provides little improvement in these Member States but increases their costs. For instance, the UK government "recognized that the Directive might give rise to 'an increased risk of litigation within the bid process, which could

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[83] McCahery & Vermeulen, *supra* note 5, at 5.
[84] Ventoruzzo, *supra* note 11, at 212.
[85] McCahery & Vermeulen, *supra* note 5, at 4.
[86] *Id.* at 6.
[87] Clarke, *supra* note 82, at 196.

have the effect of delaying or frustrating a takeover bid and hindering the opportunity for shareholders to decide upon its merits,'" and because the UK plays a prominent role in the takeover market, this problem extends beyond the UK's borders.[88] The Directive's ambiguity in many areas promotes uncertainty, which results in transactional delays as well as litigation over the meaning of such provisions. Lastly, aside from derogations by Member States, individual bidders can exclude themselves from the Directive's reach. For example, because the obligation to launch a mandatory bid does not apply when an acquirer of control in a corporation makes a voluntary bid to all shareholders,[89] by making voluntary offers, bidders can avoid the equitable price demand.[90] Loopholes like this further weaken the Directive.

For the above reasons, many have denounced the Directive as achieving a mere "soft harmonization,"[91] but the Directive's failures can largely be attributed to difficulties produced by the harmonization process itself. As can be seen, the need for consensus compromises the scope of EU legislative products, particularly given that there are pressures from all directions by numerous groups wanting to protect their existing national corporate law frameworks.[92]

Nonetheless, the Directive does have positive effects. New EU accession states could find the Directive helpful because it "provides a useful structure on which to build national takeover regulatory systems appropriate for the EU market"[93] (although Member States with existing standards could have served as substitutes for the Directive and acted as models for new Member States). The Directive also establishes a standard for measuring Member States'

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[88] *Id.* (quoting Department of Trade and Industry, *Company Law Implementation of the European Directive on Takeover Bids, a Consultative Document* (Jan. 2005), para 2.11).
[89] Directive 2004/25/EC, art. 5(2).
[90] *Application of Directive on Takeover Bids*, *supra* note 67, at 8.
[91] Ventoruzzo, *supra* note 11, at 212. *See* Gerard Hertig & Joseph A. McCaherey, *Company and Takeover Law Reforms in Europe: Misguided Harmonization Efforts or Regulatory Competititon?* (Eur. Corp. Governance Inst. Working Paper, No. 12, 2003), *available at* http://ssrn.com/abstract=438421.
[92] McCahery & Vermeulen, *supra* note 5, at 6.
[93] Clarke, *supra* note 82, at 197.

takeover regulations against those of one another because Member States—largely by choosing to opt in or to opt out—take an "explicit position on the extent to which they are willing to create a leveled-playing field in the takeover context."[94] It thus offers a common way for Member States to frame their takeover regulations and integrates the way that Member States define, refer to, and communicate about regulations in the takeover context. Perhaps this will foster better discussion about EU takeover regulation in the future given that there is a shared framework that each Member State understands and some foundation and implementation experience upon which Member States can base their proposals, suggestions, or criticisms. The Directive could also initiate competition among Member States to provide the most attractive takeover regulatory framework for corporations. As with competition among states in the U.S. to persuade companies to incorporate in their states by providing an attractive corporate jurisprudence, Member States may strive to be the Delaware of the EU in the takeover regulatory scene.[95]

V. COMPARING THE THIRTEENTH DIRECTIVE WITH U.S. TAKEOVER LAW

The European approach to takeovers seems to be very distinct from that of the U.S. Even though much of the Directive's impact has been diluted through the opt-out, it expresses a unified theoretical approach in the takeover context by the Member States (since their consensus was needed to adopt the Directive) that "confirm[s] and exacerbate[s] the divergence of the regulatory paths followed by Europe and the United States in this area of the law."[96]

At first glance, the Directive shares many similarities with the U.S. Williams Act.[97] For instance, they both require bidders to announce bids quickly, treat all target shareholders equally,

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[94] Ventoruzzo, *supra* note 11, at 213.
[95] *See, e.g.*, Robert Daines, *Does Delaware Law Improve Firm Value?*, 62 J. FIN. ECON. 525, 525-26 (2001) ("Corporate law affects firm value. Its rules determine investors' rights and managers' duties and allocate merger gains . . . Investor protection in U.S. firms varies according to the firm's state of incorporation.").
[96] Ventoruzzo, *supra* note 11, at 175.
[97] Williams Act, 15. U.S.C. § 78 (2006).

offer all shareholders the highest bid price, keep bids open long enough to allow shareholders to make an informed decision to tender, and make appropriate disclosures.[98] However, the Directive surpasses U.S. requirements and, from a U.S. perspective, breaches what is typically deemed to be the board's area of decision-making. The Williams Act does not mandate controlling shareholders to make offers, and in the U.S., "the function of protecting minority shareholders against majority oppression is principally vested in state corporate law."[99] The Directive, albeit a legislative product, can also be evaluated in comparison with U.S. case law, and doing so offers further insight into the divergence of the approaches of the EU and the U.S. For example, the Directive advocates for target boards to be passive,[100] but U.S. case law grants boards the ability to just say no to unwanted takeovers.[101] Whereas the Directive discourages defensive measures that cause a "lasting impediment"[102] to the bidder, poison pills are regularly used in combination with classified board structures in the U.S. to further deter takeovers[103]—and this defense has been approved by Delaware courts.[104] The U.S. market, by default, views all corporations as having a poison pill in place since boards can adopt them easily with a board

[98] Ferrarini & Miller, *supra* note 34, at 312.
[99] *Id.* at 313.
[100] *Id.*
[101] In *Unocal Corp. v. Mesa Petroleum Co.*, the Delaware Supreme Court created a heightened standard of review for evaluating a board's defensive response to a hostile bid: boards must "show that they had reasonable grounds for believing that a danger to corporate policy and effectiveness existed because of another person's stock ownership." 493 A.2d 946, 955 (Del. 1985). Moreover, when a company is for sale, the board has the duty to "maximize[e] [] the company's value at a sale for the stockholders' benefit." 506 A.2d 173, 182 (Del. 1986). The Court tempers the impact of *Revlon*, however, by asserting in *Paramount Commc'ns, Inc. v. Time, Inc.*, that *Revlon* duty does not trigger if a company does not seek out a transaction involving a breakup of the company and does not abandon its long-term strategy. 571 A.2d 1140, 1150 (Del. 1989). In *Time*, the target company sought out a merger with another company and then resisted high-value bids from a third party, but the Court still upheld the target board's defenses. *Id.* at 1151. Even in the face of final period situations involving concerns about directors acting in their own interests, deference is given to them. *Air Prods. & Chems., Inc. v. Airgas, Inc.* is another example of such deference; in this case, the Delaware Chancery upheld the board's ability to repeatedly refuse an offer by a hostile bidder through the use of defensive tactics. 16 A.3d 48, 127 (Del. Ch. 2011).
[102] Ferrarini & Miller, *supra* note 34, at 314 (quoting Directive 2004/25/EC, art. 9(2)).
[103] *See* Lucian A. Bebchuk, John C. Coates IV & Guhan Subramanian, *The Powerful Antitakeover Force of Staggered Boards: Theory, Evidence & Policy*, 54 STAN. L. REV. 887, 932-936 (2002);
[104] *See Air Prods. & Chems., Inc. v. Airgas, Inc.*, 16 A.3d 48, 129 (Del. Ch. 2011).

vote and without shareholder approval[105]; this is viewed as an ordinary business decision. Lastly, the Directive's breakthrough rule, while optional and requiring compensation to shareholders whose rights are broken through, "preempt[s] prior contractual and legal arrangements,"[106] an extreme regulatory step that far overreaches U.S. regulation in the takeover area.

As the above comparisons make obvious, U.S. law tends to defer to the board and give directors relatively free reign in their use of defensive tactics, but the Directive strives to give such decision-making authority to shareholders. Takeovers in the U.S. can be described as unregulated in the sense that bids are not required, there are no clear-cut rules with regard to the use of defensive tactics, and much is left to the discretion of boards—and if not them, to Delaware judges. U.S. protection of shareholders is limited to rules for the tender offer process (the Williams Act) that focus mostly on disclosure and procedural aspects of launching a tender offer.[107] The EU portrays a much more affirmative effort to keep boards in check.

This difference might be explained by the systems' different ownership distributions.[108] Some claim that because ownership in U.S. corporations is more widely dispersed than in the EU, boards are more capable of making takeover decisions,[109] but this conflicts with the reality of increasingly concentrated shareholdings of U.S. corporations in institutional investors and

[105] "It should be noted that boards may adopt poison pills, with no need for a shareholder vote of approval, not only before but also after the emergence of a hostile bid. For this reason, companies without a poison pill in place can still be viewed as having a "shadow pill" that could be rolled out in the event of a hostile bid." Lucian Bebchuk, Alma Cohen & Allen Ferrell, *What Matters in Corporate Governance?* 22 REV. FIN. STUD. 783, 792 (2008) (citing John C. Coates, IV, *Takeover Defenses in the Shadow of the Pill: A Critique of the Scientific Evidence*, 79 TEX. L. REV. 271 (2000)).
[106] Ferrarini & Miller, *supra* note 34, at 314.
[107] *See The Williams Act: A Truly "Modern" Assessment*, HARV. L. SCH. F. CORP. GOVERNANCE AND FIN. REG. (Oct. 2011), http://blogs.law.harvard.edu/corpgov/files/2011/10/The-Williams-Act-A-Truly-Modern-Assessment.pdf.
[108] Zwecker, *supra* note 75, at 254.
[109] *Id.*

mutual funds.[110] Regardless of why this distinction exists, the EU aims to enable takeovers and give a greater role to shareholders in determining whether or not an acquisition should occur. While boards in the U.S. generally have more control over the corporation when addressing a hostile bid (since, for example, there is no board neutrality rule that may apply and boards simply need to abide by their fiduciary duties), there are worries that boards may act in their self-interest, at the expense of shareholder value.[111]

But such duty of loyalty issues regarding management are always present, and it is important to note that the EU approach may actually thwart value maximization, which the Directive alleges to achieve. For instance, many Member States have opted into the board neutrality rule, which seems to produce less value than not having such a rule in place. Giving target boards the flexibility to implement takeover defenses is advantageous in many situations, particularly when they can be used as negotiating leverage against hostile bidders; boards can pressure hostile bidders to raise their offer prices because of "the threat of the defensive measures and the fear . . . that their takeover attempts will be thwarted."[112] Since the Directive prohibits target boards from frustrating a bid without shareholder approval, corporations in Member States that have adopted the board neutrality rule cannot rely on tactics like the pill to resist hostile bids that shareholders may find favorable. Moreover, because the Directive restricts bidders' freedom by allowing them to obtain control only if they launch a tender offer for all outstanding prices at a set price,[113] target corporations in the EU may receive a lower

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[110] *See* Joseph E. Bachelder III, *Institutional Shareholders and Their 'Oversight' of Executive Compensation*, THE HARV. L. SCH. FORUM ON CORP. GOVERNANCE AND FIN. REG. (July 23, 2012, 9:31 AM), http://blogs.law.harvard.edu/corpgov/2012/07/23/institutional-shareholders-and-their-oversight-of-executive-compensation/.

[111] *See, e.g.*, *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 954 (Del. 1985) ("Because of the omnipresent specter that a board may be acting primarily in its own interests, rather than those of the corporation and its shareholders, there is an enhanced duty which calls for judicial examination at the threshold before the protections of the business judgment rule may be conferred.").

[112] Zwecker, *supra* note 75, at 254.

[113] Ventoruzzo, *supra* note 11, at 174.

premium. For example, in 2007, "the average per share premium paid in merger and acquisition transactions in the United States [where there is no board neutrality rule] exceeded those in the United Kingdom (which has a Board Neutrality Rule) by approximately six percent."[114] Although other factors may contribute to this difference in per-share premium between the two's acquisitions, the distinction between their takeover regulations may be one such factor, and perhaps the data says something about the value of the U.S.'s market-oriented approach toward regulating economic activity.

VI. PROPOSALS FOR CHANGE

Since the 1960s, there has been debate over whether regulation should promote or impede takeovers,[115] and there are strong arguments on both ends of the spectrum. Takeovers can be beneficial because they replace poorly performing management and incentivize optimal performance, but they can also disrupt well-functioning companies and ignore the significance of long-term value.[116] Corporate law scholars Enriques, Gilson, and Pacces reject both positions and instead make a case for an unbiased takeover law: "[w]hile hostile and friendly takeovers may be efficient in the aggregate, individual takeovers and individual companies' exposure thereto are efficient or inefficient depending on a variety of factors."[117] The idea is that regulations should provide for individual corporations to consider their own particular circumstances.

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[114] Zwecker, *supra* note 75, at 254 (citing Brian E. Rosenzweig, *Private Versus Public Regulation: A Comparative Analysis of British and American Takeover Controls*, 18 DUKE J. COMP. & INT'L L. 213, 235 (2007)).

[115] Luca Enriques, Ronald J. Gilson & Alessio M. Pacces, *The Case for an Unbiased Takeover Law (with an Application to the European Union)* 2 (Stanford Law and Economics, Olin Working Paper No. 444, 2013), *available at* http://ssrn.com/abstract=2258926.

[116] *Id.* at 2-3.

[117] *Id.* at 3.

Enriques, Gilson, and Pacces propose that takeover law "allow individual companies to decide their degree of takeover exposure"[118] rather than attempt a one-size-fits-all solution. They thus advocate the use of "menu rules," which refer to opt-outs from a default regime.[119] The Thirteenth Directive features such menu rules, but changing which components of the Directive are subject to menu rules, as well as the scope of existing menu rules, could improve it. For example, because the mandatory bid rule can "unduly restrict takeover activity,"[120] subjecting this rule to the Directive's opt-out provision could be more value-maximizing since companies would then have the freedom to bargain for better deals when possible. Furthermore, reforming the Directive to subject the pill to a set of menu terms, rather than prohibiting its use entirely unless approved by shareholders, would make the pill regularly available for use as an effective defensive tactic and negotiating leverage while simultaneously restricting its impact.[121]

Coming up with an acceptable poison pill as a default to be employed by target boards would make the breakthrough rule more popular since there would be less need to rely on other takeover-suppressing tactics, given that the board neutrality rule, into which most Member States have opted, would enable boards to activate pills by their own discretion. The breakthrough rule could also be improved. One suggestion is to offer "a slightly different version of [it] as a menu rule"[122]; for example, it could be restructured to include a sunset clause that makes the rule effective at a specified date.[123] This would give boards flexibility to use devices like dual class shares, which enable leveraged control structures in corporations, yet the time limit provided by

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[118] *Id.* at 7.
[119] *Id.* at 23.
[120] Enriques et al., *supra* note 106, at 39.
[121] *Id.* at 44-45.
[122] *Id.* at 45.
[123] *Id.* at 46.

the sunset clause would assure the market that boards' use of the device is intended for fostering growth.

As demonstrated by some of the aforementioned ideas, perhaps the way to improve the Thirteenth Directive is to actually increase its flexibility and to bring the optionality to the company level rather than stopping at the Member State level. Perhaps the solution is not to take a pro-takeover stance (as the Directive's content currently implies) or an anti-takeover stance, but to "facilitat[e] efficient takeovers and discourag[e] inefficient takeovers."[124] To make these distinctions, if applying the framework of Enriques, Gilson, and Pacces, the Directive needs a set of menu rules structured upon a set of default rules. The problem with the Directive as it stands now is that because the default rules are "biased" in that, for instance, they attempt to eliminate the use of defensive tactics against hostile bidders, the default rules themselves have been compromised and made optional.

Were the Directive to instead provide a set of less radical rules as its pillars and then create a layer of more far-reaching menu rules, there would be a strong foundation of rules applying to all Member States (as the default) and then another layer of regulation that would trigger were States' corporations to use certain tactics or engage in certain activities. Companies would be able to assess the value of opting into such rules based on their particular circumstances. Because the harmonization process demands satisfaction by all Member States, the goal is to create a legislative product that can address a general need by creating consistency across the States—not to create a product that all Member States agree to since they can simply choose not to apply its rules. Thus, default rules, which all Member States must mandatorily abide by, should not be overly ambitious (i.e., they should be unbiased), and the rules that are optional should not weigh heavily toward any one end of the spectrum but should include terms

[124] *Id.*

and caveats to regulate and restrict the negative impacts of, for instance, defensive measures in the takeover context.