CLEARY GOTTLIEB STEEN & HAMILTON

ONE LIBERTY PLAZA
NEW YORK, N.Y. 10006

2000 PENNSYLVANIA AVENUE, N.W.
WASHINGTON, D.C. 20006-1801

41, AVENUE DE FRIEDLAND
75008 PARIS

CITY PLACE HOUSE
55 BASINGHALL STREET
LONDON EC2V 5EH

MAIN TOWER
NEUE MAINZER STRASSE 52
60311 FRANKFURT AM MAIN

RUE DE LA LOI 57
1040 BRUSSELS
TELEPHONE (32 2) 287.20.00
FAX (32 2) 231.16.61
www.clearygottlieb.com

PIAZZA DI SPAGNA, 15
00187 ROME

VIA FATEBENEFRATELLI 26
20121 MILAN

PAVELETSKAYA SQUARE 2
BUILDING 3, 10TH FLOOR
MOSCOW 115054

BANK OF CHINA TOWER
ONE GARDEN ROAD
HONG KONG

SHIN KASUMIGASEKI BUILDING
3-2, KASUMIGASEKI 3-CHOME
CHIYODA-KU, TOKYO 100-013

EUROPEAN M&A REPORT

OCTOBER - 2003

INCLUDED IN THIS ISSUE:

The next issue of the European M&A Report will appear in January 2004 and review developments that occurred in the months of October, November and December 2003.

EUROPEAN UNION

A More Coherent Contract Law in Europe – An Action Plan.

On February 12, 2003, the European Commission (the "Commission") adopted an Action Plan with a long-term strategy for achieving greater coherence of contract law in Europe. The proposed measures seek to reduce inconsistencies between and among EU and national laws and to improve the functioning of the internal market by facilitating cross-border transactions. On September 2 and September 22, 2003, the European Parliament and the EU Council respectively passed resolutions supporting the Action Plan.

Identified Problem Areas. The Action Plan presents conclusions from the first round of consultations on developing a more coherent contract law. Through the consultative process, the Commission developed a list of significant problems at both the EU and Member State levels. The problems fall into two general categories:

- *Inconsistencies in the Application of Community Law.* Community law is often applied inconsistently, causing legal uncertainty. For example, inconsistencies may stem from the absence of common definitions or the existence of overly broad definitions in EU directives, which result in inconsistency in the national implementing laws; from national legislatures maintaining existing legislation in parallel with laws implementing the directives; or from the applicability in specific circumstances of EU laws with conflicting requirements.

- *Divergent National Contract Laws*. Divergent national contract laws and the legal complexity of these divergences act as obstacles and disincentives to cross-border transactions by creating uncertainty and increasing transaction costs. For example, divergences exist in certain laws concerning the formation of contracts and the inclusion and application of standard contract terms, and in various substantive areas, such as laws relating to the transfer of property and the assignment of future receivables. These divergences are particularly problematic for small and medium-sized enterprises and consumers.

Proposed Measures. In the Action Plan, the Commission proposes a mix of regulatory and non-regulatory measures in an effort to address many of the identified problems. In addition to sector-specific directives which have been adopted and will continue to be adopted, the Commission has proposed the following broader initiatives:

- *Measure I: To increase the coherence of the EC acquis in the area of contract law*. The Commission intends to develop a "common frame of reference" with common principles and terminology to increase the coherence of existing law affecting contracts, avoid inconsistencies in the drafting of new laws affecting contracts, and enhance the uniform application of contract law in Europe, thereby facilitating cross-border transactions.[1] The resulting document, which will be publicly available, will be used by EU institutions, will serve as a reference point for the national legislatures of the Member States and possibly third countries, and will serve as a basis for reflections on whether measures, such as an optional instrument that is not sector-specific, may be needed to address problems in the area of contract law.

- *Measure II: To promote the adoption of general contract terms across Europe.* While respecting the principle of contractual freedom, the Commission intends to promote the adoption and use of standard terms and conditions. This will be accomplished by facilitating the exchange of information on initiatives that are already underway and by offering guidelines on contractual limitations under EU law, such as rules on unfair contracts terms as well as competition rules. The Commission will establish a website where individuals and companies can list information on existing or planned initiatives.

- *Measure III: To examine non-sector-specific measures such as an optional instrument.* The Commission will examine whether non-sector-specific measures, such as an optional instrument, may be needed to address problems in the area of European contract law. This will be accomplished through reflection on the desirability, possible form, possible content, and legal basis of a body of European-level contract law that could be used to facilitate cross-border transactions. Such an instrument could exist in parallel with national contract laws, and contractual parties could choose the instrument as the contract law applicable to their contract. In the spirit of contractual freedom, contractual parties could also adapt specific rules to their needs. Legal questions exist, however, as to whether such an instrument could exclude the application of conflicting national laws.

General Timetable for Action. The Commission organized two contract law workshops in June 2003. The first workshop, which focused on Measure I and, to a lesser extent, Measure III, was a forum for Member States, those States soon to be joining the European Union, and stakeholders to provide feedback on the Action Plan. The second workshop focused primarily on research projects. Later this year, the Commission plans to hold a third workshop, which will focus on Measure II. Consultations with the Parliament and the Council will continue.

---

[1] Sources to be used in developing the frame of reference include existing national law, case law of the national courts of Member *States*, established contractual practice, existing EC *acquis* and relevant binding international instruments, such as the UN Convention on the International Sale of Goods.

In a number of sectors, initiatives have already or will soon be taken to update current directives or suggest new directives. The development of a "common frame of reference" will require extensive research and input. The European Parliament has called on the Commission to complete the "common frame of reference" by the end of 2006. The Commission has stated that reflection on the optional instrument will be carried out in parallel with the other initiatives, while the European Parliament has called on the Commission to make the establishment of optional instruments in certain sectors an early priority. The European Parliament intends to hold a conference and hearing, in conjunction with the Commission, in early 2004 to discuss issues relating to the Action Plan.

UNITED KINGDOM

Cross Border Mergers: The Cases For and Against Dual Headed Structures.

Overview. Most cross-border mergers are structured using a single holding company to combine the merging companies. Occasionally, however, this conventional structure may be unacceptable since it will involve making a choice as to the new company's place of incorporation and, thus, the source of dividends paid to the combined group's shareholders. A solution that is often considered in this context is the dual headed structure, whereby the merged group is arranged under two holding companies, one in each of the two jurisdictions. Some dual headed structures involve no acquisition or disposal of shares in either of the two parent companies. Rather, each parent company retains its separate existence and listing and the two parent companies enter into contractual arrangements to ensure:

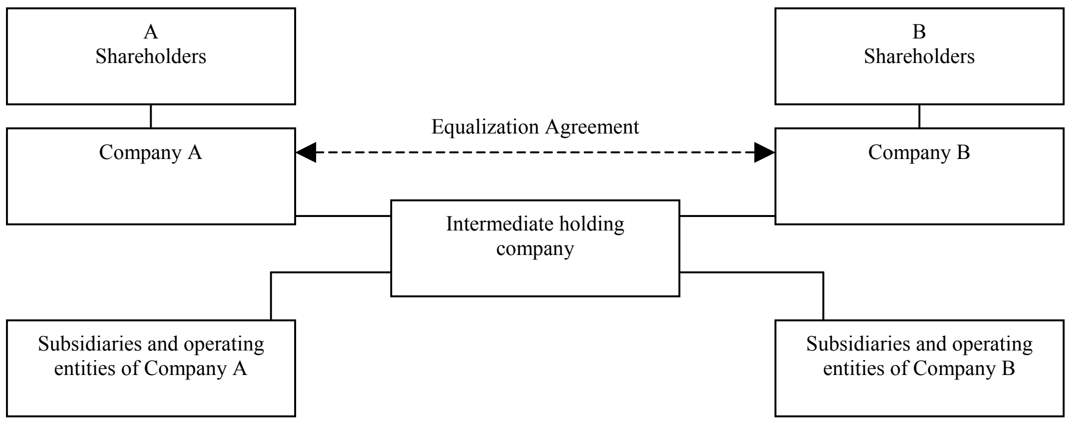
- shareholders of the two parent companies are effectively in the same economic position as they would have been if they held shares in a single combined group;
- the two companies are managed on a unified basis; and
- the companies are effectively treated as one company (*e.g.*, provisions are inserted in the companies' constitutional documents to ensure one company cannot be taken over without a concurrent offer for the other).

While dual headed structures have been used relatively sparingly over the years, they have gained prominence recently due to the mergers of BHP/Billiton, GKN/Brambles and Carnival/P&O Princess.

Although dual headed structures can be established in various ways, there are three basic models: the joint venture structure, the synthetic merger structure and the "twinned" shares structure.

(a) Joint Venture Structure

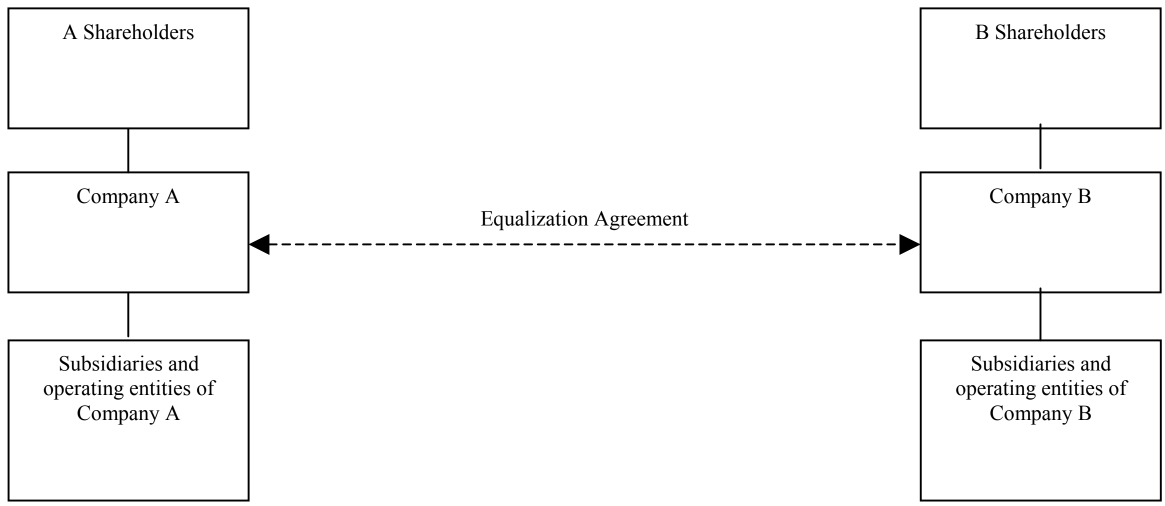
The joint venture structure involves the merging companies, Company A and Company B, transferring all of their assets to one or more intermediate holding companies, in which each of Company A and Company B holds shares. Each of the merging companies retains its separate existence and its shares trade separately. Many mergers have employed this structural approach, including the Royal Dutch/Shell and Reed/Elsevier transactions.



(b) Synthetic Merger Structure

If the joint venture structure is too difficult or costly to implement, the parties may employ the synthetic merger structure. Under this structure, the merging companies retain full ownership of their respective business operations and there is no intermediate holding company with businesses beneath it.

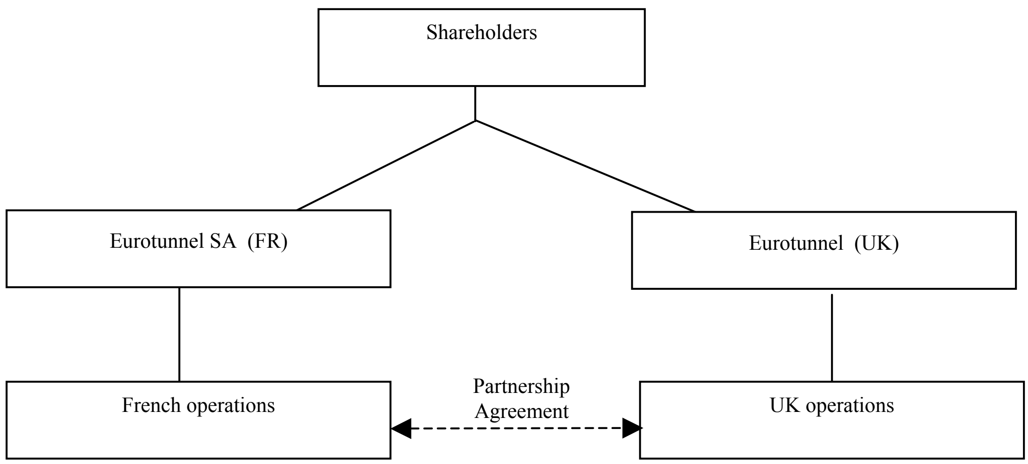
The synthetic merger structure was used in the recent BHP/Billiton, GKN/Brambles and Carnival/ P&O Princess mergers.



(c) Twinned Shares Structure

The "twinned" share structure, typified by the Eurotunnel merger, provides that the merged group is owned by two holding companies, Company A and Company B.

The shares of each are stapled together and are owned and traded by investors as a single unit to avoid price differentials between the two shares when traded separately.



Advantages

- *National Identity*. Factors such as national pride, governmental pressure or the desire to remain eligible for a particular index, may make it unacceptable for the holding company of a group to move to another jurisdiction. The continuity of corporate identity and domicile in these circumstances may make a dual headed structure more palatable to interested parties who may feel that this structure is more appropriate for a combination touted as a "merger of equals".

- *Shareholder Approval*. Implementation of a dual headed structure would normally require shareholder approval for any changes to the parties' respective constitutional documents to ensure the two groups act in a unified manner post-merger. Threshold percentages to approve charter amendments are typically lower than thresholds required to effect a squeeze out in the context of a takeover. For example, a takeover offer for a U.K. company (unless effected as a scheme of arrangement) would require acceptances from 90% of the shares to which the offer relates before the offeror has the right to squeeze out the remaining minority, while a U.K. company involved in a dual headed structure would require only 75% of the votes cast at a shareholders meeting to approve amendments to its constitutional documents.

- *"Flowback"*. A complexity often associated with a single holding company structure is "flowback". Where the acquiring company is listed or incorporated in another jurisdiction and the target drops out of a stock exchange index as a result of the merger, many institutional investors, pension funds and tracker funds will sell their shares. These sales cause significant "flowback" of shares to the other jurisdiction and could turn what was intended to be a no premium merger into a takeover at a discount. A dual headed structure minimizes this problem by enabling shareholders to continue to hold shares in a company incorporated and listed in their local jurisdiction.

- *Change of Control*. The synthetic merger structure may avoid triggering change of control provisions in joint venture or other commercial agreements. This is sometimes an important advantage as such provisions can threaten to undermine the value and rationale of the merger.

- *Tax*. From a tax perspective the principal advantage of a dual headed structure is obtained when it enables shareholders to receive "tax advantaged dividends". This may occur where shareholders are resident in the same jurisdiction as one of the companies and are able to receive tax credits attaching to dividends or where the dividends are tax exempt when paid by the company in that jurisdiction (in contrast to dividends from other jurisdictions which may be taxable and/or subject to withholding tax). The loss of these tax credits could be sufficient to prevent shareholders from approving a merger. This was one of the issues in the BHP/Billiton merger, as Australian shareholders benefit from a franking credit when they receive dividends from an Australian company. A dual headed structure may also be attractive where capital gains rollover is not available in respect of a conventional merger for shareholders in one or both of the relevant jurisdictions. Under the joint venture and the synthetic merger structures, a shareholder continues to own the same shares, so there should be no taxable event for capital gains tax purposes.

- *Future Acquisitions.* A dual headed structure may give a certain amount of flexibility with respect to future acquisitions, as the shares of either parent company could be used as acquisition currency. However, there are difficulties with this where a twinned share structure is used. In this structure, the shares of both parent companies are stapled together and each holding company would have to acquire part of the target in return for an issue of the stapled stock.

Disadvantages

- *Dual Regulatory Regimes*. Each of the two parent companies will remain subject to the laws and regulatory regimes of its jurisdiction of incorporation. This can lead to conflicts between the corporate laws applicable to the merged group. There are usually complex provisions in dual headed structures dealing with company law rules and corporate governance principles to ensure the merged company can act in a unified manner post-merger. Changes are often made to the constitutional documents to ensure that the shareholders of both parent companies act on a combined basis with respect to certain corporate matters affecting the shareholders of each company in a similar way (*e.g.*, appointment of directors and adoption of accounts). This has been achieved in synthetic merger structures by means of each company issuing a special voting share which is cast by a special voting company set up for these purposes. Each special voting share will carry the same number of votes as are cast for and against the equivalent resolution at the other company's shareholders meeting. On other matters where the two sets of shareholders may have divergent interests, such as a change in the corporate status of a parent company or changes to the dual headed structure documents, the special purpose company will only vote the relevant special voting shares if the equivalent resolution has not been passed at the other company's shareholders meeting and will have sufficient votes to defeat the proposed resolution. Other changes to the constitutional documents might involve provisions to ensure that the two parent companies maintain identical boards. These provisions can prove complex and cumbersome in practice. An additional consequence of the layers of complexity in a dual headed structure is that it may lead to a misunderstanding among investors. Different accounting rules of the different jurisdictions and equalization agreements may confuse investors and lead to a misunderstanding of the financial results of the group.

- *Implementation Flexibility*. The complexity of a dual headed structure can lead to difficulties during implementation, particularly when there is the prospect of a competing bid. Flexibility, which is so often required in these situations, is limited. For example, reacting to a competing bid would invariably require the necessary shareholders meeting to be adjourned and the restructuring of an already complex transaction. Unlike in a dual headed structure, a U.K. takeover offer for a U.K. target can, of course, proceed without the recommendation of the target company and it is relatively straightforward to vary and improve the terms of the offer if a competing bid has been launched. Implementation of a dual headed structure is typically on a merger of equals basis (*i.e.*, no premium is paid to either side). Although feasible, it is relatively complex and unprecedented to date, for one party to pay a cash component to shareholders of the other side as a premium for the merger. Hence, varying the consideration terms of a dual headed structure (*e.g.*, to include a cash component to make the merger more attractive) in order to react to a competing bid or for other reasons is troublesome. This inherent inflexibility was highlighted recently when Royal Caribbean/P&O Princess attempted to implement a dual headed structure and the initiative was taken by Carnival when it launched a takeover offer for P&O Princess (Carnival's offer was later transformed into a dual headed structure and Carnival was ultimately the successful bidder).

- *Tax*. Depending upon the precise dual headed structure adopted, it may be necessary for the two groups to enter into an equalization agreement. Under such an agreement each company pays dividends in accordance with a pre-agreed equalization ratio, ensuring that the shareholders will be in the same economic position as if they held shares in a single combined enterprise. If one parent has insufficient funds to make a proposed distribution, the equalization agreement enables the other parent company to make an equalization payment to fund the shortfall. From a corporate tax perspective, payments under an equalization agreement can be inefficient. This is because in many jurisdictions the receipt of a payment under the equalization agreement would be treated as a taxable receipt, whereas the payment would not be deductible. Care also should be taken with tax residence issues which may arise where the two parent companies have identical boards and effective joint management. This is because in many jurisdictions a company may be tax resident, and thus its income taxable, in a jurisdiction if it is effectively managed there even if it is incorporated elsewhere.

- *Share Price Discrepancies.* The joint venture and synthetic merger structures are susceptible to share price discrepancies between the two parent companies which can arise for a variety of reasons (*e.g.*, differences on tax treatment of dividends, as a result of the different stock market index membership of the parent companies, or, perhaps, as a result of the different currencies in which the shares trade). This is a common problem and can cause difficulties in pricing new equity issues, such as a rights issue. For example, Fortis, which was a Dutch/Belgium dual headed joint venture structure formed in 1990, became a twinned share structure in 2001. One of the main reasons for this was the permanent difference in market values of the shares in the two parent companies that had developed. The new Fortis structure, and twinned share structures generally, avoid arbitrage trading in the parent companies' shares.

- *Market Capitalization.* The twinned share structure of Fortis resulted in a single listed entity with a combined market capitalization. Previously, due to the existing dual headed structure, Fortis Belgium and Fortis Netherlands were only included in major share indices at their individual market capitalizations, so the group had not fully benefited from its market size. In a joint venture or synthetic merger structure, the two parent companies are considered separately for stock market index membership, with the result that the combined group's over all market capitalization is divided.

- *Cost Savings and Synergies*. In many mergers, the principal rationale and justification for the merger is the cost savings and synergy benefits that are expected. With dual headed structures it is more difficult to realize these cost savings and synergies than with a conventional single holding company structure. Clearly, as can be seen from the synthetic merger structure diagram above, the two limbs of the "merger" are, for all intents and purposes, separate rather than combined as in a true merger. One of the main benefits of the joint venture structure is that it allows for a combination of the two groups at the operating level with a potentially greater realization of synergies as compared to other dual headed structures.

- *Takeover Protection*. Dual headed structures often employ protective provisions in each of the companies' constitutional documents to prevent or make unattractive a takeover bid for one parent company without an accompanying bid for the other. While these provisions may be helpful to the unity of the dual headed structure, they may also have the negative effect of reducing the attractiveness of the group to a third party.

Conclusion

In many cases, dual headed structures can be considered a step in the evolution of a group for which full unification is the ultimate goal. Dual headed structures often involve the merger of two well established and developed groups with strong domestic links. The structure allows such companies to merge while maintaining some degree of independence and permits shareholders time to become accustomed to the before further changes are made on the road to full unification. This trend towards unification has been typified in recent years by groups such as Allied Zurich, ABB (the combination of ASEA and BBC Brown Boveri), Dexia and Fortis moving away from dual headed structures towards either full unification under one group company or partial unification, as in the case of Fortis, by creating a new single listed security of twinned shares.

Nevertheless, the longevity of some dual headed structures, such as Royal Dutch/Shell and Unilever, seem to suggest the contrary (*i.e.*, that a dual headed structure can work in the long term and can overcome its shortcomings). This fact, combined with the recent popularity of dual headed structures (*e.g.*, BHP/Billiton, GKN/Brambles and Carnival/P&O Princess), would seem to suggest that dual headed structures are alive and well.

GERMANY

Reform of Appraisal Proceedings.

On September 1, 2003, the Act on the Reform of Appraisal Proceedings (*Spruchverfahrens-neuordnungsgesetz*) entered into force. The Act establishes a uniform set of procedural rules for appraisal proceedings, the Appraisal Proceedings Act (*Spruchverfahrensgesetz*), applicable to different types of corporate reorganization measures, and also introduces changes to the Stock Corporation Act (*Aktiengesetz*) and the Transformation Act (*Umwandlungsgesetz*). The new legal regime is designed to address the legal, technical and practical shortcomings of the previously applicable rules, namely: (i) the lack of a comprehensive regulation of appraisal proceedings in a single statute, (ii) the long duration of appraisal proceedings (five years on average), and (iii) the time-consuming reliance on newly appointed valuation experts during the appraisal proceedings.

General. Minority shareholders of a German stock corporation are entitled to receive adequate cash compensation in connection with certain reorganization measures affecting the corporation in which they hold a stake. This is the case with respect to (i) minority shareholders of a controlled company entering into a domination and/or profit transfer agreement, (ii) minority shareholders of a stock corporation being integrated with another stock corporation, (iii) the squeeze-out of minority shareholders, and (iv) minority shareholders of stock corporations that are the subject of corporate transformation acts, such as mergers, spin-offs and changes of the corporate form. In essence, a minority shareholder has two options for protecting its rights in such a corporate reorganization situation. First, a shareholder may bring an action against the shareholders' resolution approving the reorganization measure, requesting that the court set aside the relevant resolution. A successful challenge of the shareholders' resolution prevents the reorganization measure from becoming effective. Such action may only be based on a violation of the formal legal requirements applicable to the calling of the shareholders' meeting or the adoption of the shareholders' resolution approving the relevant measure. A minority shareholder may not, however, challenge the validity of such a shareholders' resolution based upon a claim that the cash compensation offered was not adequate. This type of challenge can only be brought in special appraisal proceedings, which is the second opinion available to a minority shareholder. The institution of appraisal proceedings does not affect the validity of the shareholders' resolution approving the corporate reorganization.

Court-Appointed Valuation Experts. Under the new legal regime, the valuation experts who will perform the initial review of the cash compensation offered to the minority shareholders (based upon a valuation of the company or companies concerned) will be appointed by the competent court rather than by the companies implementing the reorganization measure.[2] This change is intended to enhance shareholder confidence in the valuation report and to limit the need for the appointment of new valuation experts in subsequent appraisal proceedings. Under the previously applicable rules, it was common practice that upon the commencement of appraisal proceedings, the court appointed a new valuation expert to perform a full-fledged re-valuation of the company and re-calculation of the cash compensation offered to the minority shareholders.

Commencement of Appraisal Proceedings. A minority shareholder who wants to challenge the cash compensation offered must initiate the appraisal proceedings by lodging a complaint with the competent court within three months after the entry of the relevant reorganization measure into the commercial register. The complaint must substantiate the objections against the valuation of the company and the resulting determination of the cash compensation.

Obligation to Further Appraisal Proceedings. Under the Appraisal Proceedings Act, the court no longer engages in a comprehensive *ex officio* investigation of all relevant facts. The burden to present the facts is placed primarily on the parties to the appraisal proceeding. The Appraisal Proceedings Act also provides that every defendant is required to respond in writing to complaints within a short response period set by the court, which period shall be no shorter than one month and no more than three months. The court may accept late responses only in a limited number of cases (*e.g.*, in the event that the response is unlikely to result in a delay of the appraisal proceedings or if the defendant presents an adequate excuse for the delay). Otherwise, late responses will be rejected.

Furnishing of Information. As a further means to accelerate the proceedings, the Appraisal Proceedings Act imposes various obligations on the defendant to submit documents to the court and the claimant. First, the defendant is required to submit to the court (and at the claimant's request also to the claimant) the report of the management board on the reorganization measure and the valuation report prepared by the valuation experts. Second, at the request of the court or the claimant, the defendant is obligated to submit to the court or any expert retained by the court all documents that may be relevant for the decision of the court, including internal valuation reports prepared by the defendant and working papers of the valuation experts. To the extent such documents contain confidential information, the documents shall not be made available to the claimant (so as to safeguard manufacturing, operating or business secrets).

---

2 In anticipation of the then already contemplated changes of the regime applicable to appraisal proceedings, the squeeze-out rules that entered into force at the beginning of last year already required that the squeeze-out cash compensation offered to minority shareholders be reviewed by a court-appointed valuation expert.

Finally, the court may at any stage of the proceedings request supplemental information, including internal notes, from the claimant and the defendant.

Mandatory Hearing. Under the Appraisal Proceedings Act, the competent court is required to hold a hearing before it makes a final decision. As opposed to the previous regime, the court will generally also have to hear from the valuation experts that performed the initial valuation of the company or companies concerned and the cash compensation to be offered to minority shareholders.

In-Court Settlements. The new legal regime actively encourages in-court settlements. The court must at all stages of the proceedings be supportive of an in-court settlement by the parties.

Effect of Final Decisions. The final non-appealable court decision in an appraisal proceeding is effective for and against all minority shareholders affected by the relevant reorganization measure, including those who accepted any initial (lower) cash compensation offered. In the event of a court decision in favor of the minority shareholders, those minority shareholders who accepted an initial lower cash compensation will receive the difference between the cash compensation awarded by the court and the one initially paid to them.

FRANCE

First Application of New Takeover Regulations Allowing Conditionality on Competition Authority Approval.

The recent tender offer by Alcan Inc. ("Alcan") of Canada for the French steel company Pechiney represents the first tender offer in France to take advantage of amendments to Title V of the General Regulations of the *Conseil des marchés financiers* (CMF), described in the October 2002 and January 2003 editions of the European M&A Report. Those amendments allow, *inter alia*, tender offers for securities listed or publicly traded in France to include the receipt of necessary approval from the relevant competition authorities as a condition precedent to satisfaction of the offer. In this case, the Alcan offer included a condition whereby the offer would automatically lapse if the proposed transaction became subject to Phase II review by the European Commission (the "Commission") or any similar review by the relevant national authorities to whom the Commission had referred the transaction or by the United States antitrust authorities.[3] In addition, the launch of the offer was subject to the standard requirement of prior approval by the CMF and, due to Pechiney's involvement in the defense sector, by the French Minister of the Economy, Finance and Industry. Given the timing of the receipt of the various regulatory approvals, the competition condition was, in fact, satisfied by the time Alcan formally launched the offer on October 7, 2003.

The bid by Alcan revived the failed merger attempt by Alcan, Pechiney and algroup of Switzerland in 1999 and early 2000 (the "APA merger"), which was blocked by the competition authorities. Following that attempt, Alcan and algroup merged without Pechiney in late 2000. This time, Alcan conducted preliminary discussions with the Commission prior to finalizing its offer for Pechiney in an attempt to avoid a recurrence of the objections that led to the APA merger not being completed. In 2000, Alcan was unwilling to sell certain key assets and this refusal resulted in the principal competition concerns that ultimately blocked the transaction. This time, Alcan indicated its flexibility as to ownership of certain assets and its willingness to consider possible divestitures in segments that could have been a source of concern.

Alcan originally filed the notification of its offer for Pechiney with the Commission on August 14, 2003. Since the standard one-month review period is extended to six weeks if the notifying party offers to agree to divestitures or other obligations that would eliminate significant competition concerns (which was the case here), the period for Phase I review by the Commission continued until September 29, 2003.[4]

On that date, the Commission approved the transaction, subject to the sale of certain European assets of the combined entity. The Commission reported Alcan had also agreed to eliminate overlaps in other markets, to continue licensing certain identified technologies and to divest one

---

[3] If the offer lapsed due to this condition not being met, Alcan reserved the right to commence a new offer. In addition, Alcan reserved the right to proceed with the initial offer even though it may have been required to comply with certain conditions or obligations imposed by the relevant competition authorities.

[4] In order to take advantage of the amended Title V regulations of the CMF, Alcan was required to deliver to the CMF a copy of its filing with the relevant competition authorities and to keep the CMF informed of progress in the competition review process.

other technology. On September 29, 2003, Alcan also received approval for the transaction from the U.S. antitrust authorities, subject to the sale of certain assets within the U.S. market. The necessary approval of the French Minister of the Economy, Finance and Industry was received on September 5, 2003and the CMF granted its approval of the offer on September 29, 2003.[5] Assuming no further delays, the offer period is expected to close in late November 2003.

French Corporate Governance Update.

The sponsors of the recent private sector recommendations on corporate governance, the *Rapport Bouton* presented on September 23, 2002, and the two previous *Rapports Viénot*, are in the process of publishing a consolidated report regarding corporate governance standards. This consolidated report is intended to serve as France's "reference code" for corporate governance, as mandated by the European Commission.

In conjunction with the preparation of the consolidated report, the *Association Française des Entreprises Privées* (AFEP), a professional organization that participated in preparing the *Rapport Bouton*, has conducted a survey that reviews the adoption by French companies of the recommendations made by the *Rapport Bouton*. The survey, entitled "One Year After the *Rapport Bouton*," reviews the 2002 annual reports of the CAC 40 companies (a group of 40 of the largest companies in France, selected on the basis of size of market capitalization and liquidity) and the adherence of these companies to the recommended corporate governance standards.

The survey concludes that the CAC 40 companies have, on the whole, generally applied the principles of corporate governance contained in the consolidated report. In particular, the provisions regarding disclosure of risks and off-balance sheet commitments, creation of specialized committees and publication of information regarding officers and directors were well observed. Approximately half of the companies have adopted the recommendations regarding the composition of the board of directors and the percentage of independent directors on certain board committees.[6] Many of the companies, however, have not yet published the ratings they receive from rating agencies or adopted formal internal regulations for the organization of their audit committees and the organization and evaluation of the board of directors.

For a description of the *Rapport Bouton,* see the May 2003 edition of the European M&A Report. If you would like to receive a copy of the survey results, please send an email to clearygottlieb@cgsh.com.

European Commission Agrees to Alstom Plan.

On September 22, 2003, the European Commission approved a modified plan to restructure the French company Alstom. In the face of a decision by Brussels to enjoin the previously proposed plan in which the French government would have taken an equity stake in the shareholding of Alstom, a modified plan was agreed in which the French state will provide medium- and long-term subordinated financing to Alstom amounting to €800 million. Such financing, some of which could be repaid in the form of Alstom shares, includes:

- subordinated notes aggregating €300 million and having a term of 20 years (these notes will be repayable in the form of Alstom shares if the European Commission confirms that the issuance of such notes and their conversion into shares is compatible with EU rules and does not represent illegal state aid);

- subordinated notes aggregating €200 million and having a term of 15 years (which notes will be repayable in cash); and

- a conventional subordinated loan of €300 million having a term of 5 years.

---

[5] Initially, Alcan had insisted on a cash ceiling on the value of the bid regardless of the value of the Alcan shares at the time the offer was completed. It was only following Alcan's agreement to various adjustments and assurances from the investment banks advising Alcan that the offer could not fall below certain value thresholds that the CMF approved the offer.

[6] Many of the companies surveyed commented that they intended to achieve the recommended number of independent directors (*i.e.,* one half) on their boards progressively, as incumbents are replaced. Only a minority of the companies surveyed had adopted the recommended limitation of four years on the term of office of directors.

The overall restructuring plan, three-quarters of which will be financed by French and international banks, is estimated to have a value of €3.2 billion.

ITALY

A Window On the Reform of Italian Corporate Law (Part II): New Rules on Corporate Governance Structures.

In January 2003, the Italian government approved a wide-ranging reform of the corporate law provisions of the Civil Code (the "Reform"), which will become effective on January 1, 2004. We provided a general description of the Reform in the October 2002 edition of the European M&A Report, and in the July 2003 edition we focused on the key new rules regarding shareholders' agreements and segregation of assets. In this Report, we examine the main features of the three corporate governance structures that the Reform permits for Italian stock companies.

The Reform provides that any stock corporation may choose to establish (i) a traditional Italian governance system with a board of directors and a board of statutory auditors (*collegio sindacale*); (ii) a two-tier governance system with a management board and a supervisory board; or (iii) a one-tier governance system with a single board which includes an audit committee. If a company does not explicitly choose to adopt one of these options, the traditional Italian governance system will apply by default.

Traditional System. Under the traditional system, as set forth in the Reform, a company must have a board of directors and a board of statutory auditors.

Responsibilities. The board of statutory auditors is responsible for carrying out control activities. The board generally will no longer be responsible for the audit of the annual accounts, which will be performed by an external auditor. There is an exception for companies that (i) are not obliged to prepare consolidated financial statements and (ii) do not have recourse to equity capital markets (*i.e.*, whose shares are not listed on a regulated market or that do not have a shareholders' equity of at least €5 million and more than 200 shareholders). In this case, companies may still assign such responsibility to the board of statutory auditors in order to reduce administrative costs.

Election; Composition; Independence. The members of the board of statutory auditors must be elected at the shareholders' meeting. The board must consist of three professional auditors,[7] each of whom is independent. The following persons are not considered independent and are prohibited from being members of the board of statutory auditors: (i) persons who have been declared unfit, incompetent or bankrupt by a court; (ii) persons who are connected to the company or its affiliates through an employment contract, a consultancy agreement or any kind of paid services; and (iii) persons who are related to the directors of the company or its affiliates.

Applicability. The choice of the traditional system may be suitable for non-listed companies.

Two-Tier System. Under the two-tier, German-style system, a company is governed by an administrative body (the management board) and a control body (the supervisory board).

Responsibilities. The responsibilities of the supervisory board are similar to those of the board of statutory auditors under the traditional governance system, but also include additional responsibilities, such as appointing and removing the members of the management board, approving the financial statements (subject to certain exceptions), bringing derivative suits against the members of the management board, and determining the compensation of the members of the management board (unless the company's by-laws provide that such compensation be set at the shareholders meeting). The supervisory board cannot be charged with the duty to audit the company's accounts, which is a mandatory responsibility of the external auditor.

Election. Members of the supervisory board are elected at the company's shareholders' meeting. The shareholders have the right to recall supervisory directors by a resolution approved by shareholders representing at least one-fifth of the outstanding capital stock. However, any shareholder who is a member of the management board may not vote upon a resolution to appoint or recall any supervisory director.[8]

---

7 A professional auditor is defined as a person enrolled in the registry of auditors held by the Ministry of Justice.

8 Note that in the event of a disagreement among shareholders regarding appointments to the supervisory board, a majority shareholder who actively participates in the management of the company and has not assigned his

Composition. The supervisory board must have at least three members, of whom at least one must be a professional auditor. This may provide companies implementing the two-tier system with a slight advantage over those using the traditional Italian system in terms of possible reductions in cost, because only two professional auditors (one member of the supervisory board and the external auditor) will be required, as opposed to the three auditors (if no external auditor is required) or four auditors (if an external auditor must be appointed) required under the traditional Italian system.

Independence. The independence criteria for members of the supervisory board under the two-tier system are similar to those for members of the board of statutory auditors under the traditional system. Under the two-tier system, the following persons are not considered independent and are prohibited from being members of the supervisory board: (i) persons who have been declared unfit, incompetent or bankrupt by a court; (ii) persons who are connected to the company or its affiliates through an employment contract, a consultancy agreement or any kind of paid service; and (iii) persons who are part of the management board.

Applicability. The choice of the two-tier governance system may be suitable for:

- companies in which no single shareholder or coalition of shareholders holds one-fifth or more of the share capital (because of the one-fifth threshold necessary to recall the members of the supervisory board);
- companies intending to acquire entities incorporated in jurisdictions which require a two-tier system, such as Germany or Holland, or intending to participate in joint ventures with such entities in order to facilitate post-acquisition or joint venture governance arrangements; and
- companies in which management and ownership are separated to enable ownership actively to supervise the management without taking on management responsibilities (*e.g.*, family-owned businesses that decide to entrust management to specialists outside the family).

One-Tier System. Under the one-tier, U.K./U.S.-style governance system, a company must have a single board of directors and an audit committee that meet certain requirements.

Independence of Board. At least one-third of the directors must be independent. The criteria for independence are the same as those for the board of statutory auditors of companies adopting the traditional Italian system. That is, the following persons are not considered independent and are prohibited from being members of the board of statutory auditors: (i) persons who have been declared unfit, incompetent or bankrupt by a court; (ii) persons who are connected to the company or its affiliates through an employment contract, a consultancy agreement or any kind of paid services; and (iii) persons who are related to the directors of the company or its affiliates.

Appointment; *Composition; Independence of Audit Committee*. Unless the company's by-laws provide that the members of an audit committee be appointed by the shareholders at a shareholders' meeting, the board is required to appoint the committee from its own members. Companies that have recourse to equity capital markets must have at least three members, and other companies must have at least two members. These members must all be independent, as defined above, and may not be entrusted with managerial obligations or functions connected with managing the company or its affiliates. At least one member must be a professional auditor.

Responsibilities of Audit Committee. The committee is responsible for carrying out control activities similar to those performed by the statutory auditors in the traditional Italian system. As in the two-tier model, the audit of the company's accounts is a mandatory responsibility of the external auditors.

Suitability. The one-tier model system may be suitable for listed companies, which under the best practice rules of the Italian stock exchange should in any event have independent directors and an audit committee. An exception would be companies listed only or also in the United States that may wish to avail themselves of an exemption available to companies with a board of statutory auditors meeting defined criteria, from certain of

---

shares to a third party (*e.g.,* a holding company), may not vote on such appointments. This would *de facto* leave minority shareholders with the ability to control the membership of the supervisory board, which, in turn, has the power to elect and recall the members of the management board.

the audit committee independence requirements imposed on issuers by Section 301 of the Sarbanes-Oxley Act of 2002 and the rules promulgated thereunder.

Conclusion. An understanding of the particular characteristics of each of these governance systems will be important for lawyers advising clients on potential structures for M&A transactions involving Italian companies, particularly transactions involving joint venture entities and transactions where the resulting entity will have minority shareholders.

THE NETHERLANDS

Second Chamber Adopts Proposal to Amend Dutch Corporate Law.

On September 9, 2003, the Second Chamber (*Tweede Kamer*) of the Dutch Parliament adopted a bill proposing additional rights for the general meeting of shareholders and holders of depository receipts, and certain amendments to the "large company rules" (*structuurregime*).[9] The proposal will now be considered by the First Chamber (*Eerste Kamer*). If, as seems likely, the proposal is adopted by the First Chamber within the next few months, it will come into effect in early 2004.

Given that the Dutch government has previously announced that it will conduct a more fundamental review of the large company rules in the near future (a review which may lead to additional and potentially far-reaching changes to the large company rules), this present proposal may be partially overtaken by later changes. In addition, as discussed in the July 2003 edition of the European M&A Report, a new corporate governance code is intended to be finalized towards the end of this year and to take effect as of January 1, 2004.

The following is a brief summary of certain key elements of the proposed bill.

Additional Rights for the General Meeting of Shareholders. Under the proposed bill, the general meeting of shareholders will have additional rights, including the following:

- *Shareholder Approval for Major Transactions.* Shareholders will need to approve resolutions of the management board that change the company's character or identity in an important way, including the transfer of all or substantially all of the company's business, the entering into or termination of long-lasting joint ventures, and the acquisition or disposal of assets of the company which have a value at least equal to one third of the company's consolidated net worth.

- *Shareholder Proposal Rights.* Shareholders representing at least one percent (1%) of the outstanding capital (or, if the company is listed, at least €50 million), will have the right to request the inclusion of additional items on the agenda of the general meeting and only in certain limited instances may the company refuse to include such items.

- *Approval of Directors' Remuneration.* Shareholders will need to approve a comprehensive remuneration policy for members of the management board, including provisions on bonuses, stock options and severance payments. In the event the actual remuneration of the members of the management board is not set by the shareholders, the supervisory board or other responsible corporate body will be required to adhere to the policy. Under the proposed bill, the remuneration of the members of the supervisory board itself must be determined by the shareholders.

Voting Rights for Holders of Depository Receipts. Under the proposed bill, changes will be made to the Dutch practice of issuing depository receipts. As discussed in the July 2003 edition of the European M&A Report, depository receipts are listed instruments issued by a special purpose foundation (*administratiekantoor*) that carry rights to the beneficial ownership of underlying shares (in a specific company) held by the foundation.[10]

---

9 The "large company rules" require companies of a certain size to adopt, absent an exemption, a two-tier board structure in which the supervisory board appoints its own members, through a system of co-optation, and the members of the management board.

10 Approximately 20% of all Dutch companies listed at Euronext Amsterdam are listed through depository receipts. The issuance of depository receipts is one of the three anti-takeover measures that are most commonly employed by Dutch companies.

They are either fully exchangeable for the underlying shares or, as is more common, exchangeable for a certain maximum percentage of the underlying shares. Crucially, it is the foundation and not the holders of the depository receipts that exercises the voting rights attached to the underlying shares. Under the proposed bill, holders of depository receipts would be given the right to demand an exclusive (*privatieve)* power of attorney to exercise the voting rights attached to the underlying shares. The issuing foundation could refuse to provide or, if already provided, could subsequently revoke, this power of attorney, only if (i) a hostile public offer for the underlying shares has been made or announced, or it is reasonably expected that such an offer will be announced in the near future, (ii) the depository receipt holder, acting alone or in concert with others, represents 25% or more of the company's issued share capital, or (iii) the issuing foundation believes that the holder of the depository receipt would cast a vote that would seriously prejudice the best interests of the company or the company's business.

Appointment of Members of the Supervisory Board. Under the large company rules, the supervisory board appoints both its own members (through a system of co-optation) and the members of the management board. Under the proposed bill, the general meeting of shareholders will be granted the power to appoint the members of the supervisory board, although the supervisory board will have the right to nominate candidates according to a general "profile" for supervisory board members (the "profile" having been previously established by the supervisory board following discussions with both the general meeting and the works council). Provided that at least one-third of the issued capital is represented, the general meeting will have the right, by a two-thirds vote, to reject any candidates proposed by the supervisory board. If this quorum requirement is not met, a simple majority vote at a second meeting will suffice to reject a supervisory board's candidate.

In addition, under the proposed changes the works council will be entitled to present candidates for the supervisory board for at least one-third of the vacant positions.[11,] If the supervisory board rejects the candidates proposed by the works council, the supervisory board and the works council should try to reach an agreement with respect to the proposed candidate or another candidate. In case the supervisory board and the works council fail to reach an agreement the Enterprise Chamber (*Ondernemingskamer*) of the Amsterdam Court of Appeal (the "Enterprise Chamber") will have to decide whether or not the supervisory board's objections to the proposed candidate were reasonable. As in the case of the candidates proposed by the supervisory board, the general meeting of shareholders will have the right to reject the work council's candidates in accordance with the procedures described above.

The general meeting of shareholders will also have the right, by a simple majority vote (provided at least one-third of the issued capital is represented), to dismiss the entire supervisory board (but not any individual member). In such a case, the Enterprise Chamber will then appoint a temporary supervisory board that will propose new supervisory board members.

Finally, the supervisory board, the general meeting of shareholders and the works council may agree on an alternative arrangement for the appointment of supervisory board members, provided that the arrangement does not limit the right of the general meeting to reject candidates, as described above.

---

11 If the number of seats on the supervisory board cannot be divided by three, the resulting number will be rounded down. The proposed bill contains a transitional provision which requires that each second vacancy in the supervisory board that arises after the proposal takes effect will be subject to the works council's recommendation right until one-third of the members of the supervisory board has been appointed on the works council's recommendation. In anticipation of the adoption of this proposal several companies and, in particular, a number of Dutch multinationals that had adopted the large company rules on a voluntary basis, have changed their articles of association (*i.e.,* withdrawn from the application of the large company rules, as is possible for Dutch international holding companies) so as to exclude any right of the works council to present candidates for nomination to the supervisory board. These multinationals take the view that, since a majority of their workforce is based outside the Netherlands, it would be problematic for the Dutch works council, which in practice represents Dutch employees only, to have significant influence over the composition of the supervisory board.

For more detailed information concerning any items in this Report, please contact any of the following persons:

<u>Brussels Office</u>
Jacques Reding
Tom W. Cox
Laura Black

<u>Paris Office</u>
Jean-Marie Ambrosi
Pierre-Yves Chabert
Bruce McCoy

<u>Rome Office</u>
Giuseppe Scassellati
Stefano Sciolla

<u>London Office</u>
Simon Jay
Matthew D. Barton

<u>Frankfurt Office</u>
Thomas Buhl
Klaus Banke

clearygottlieb@cgsh.com