An Institutional Analysis of
Cross-border Hostile Takeovers

Shareholders value, short-termism and regulatory arbitrage on the Swedish stock market during the sixth takeover wave

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To
My Family

Foreword

This volume is the result of a research project carried out at the Center for Management and Organization at the Stockholm School of Economics (SSE).

This volume is submitted as a doctor's thesis at SSE. In keeping with the policies of SSE, the author has been entirely free to conduct and present her research in the manner of her choosing as an expression of her own ideas.

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Stockholm, October 2012

Sophie Nachemson-Ekwall

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Chapter 1

Introduction

1.1 Background

During the period 2004–2008, generally described as the *sixth takeover wave*[1], Europe experienced a number of takeovers. The activities coincided with a period of high growth in the world economy, low interest rates, high leverage and expansion of credit in the economy. Statistics give a clear picture of the takeover frenzy during the boom-years of the sixth takeover wave. In 2004, global takeovers accounted for 2.7 trillion dollars, up by 40 per cent compared to the previous year (Davidoff, 2009, p.16). By 2007, this number had grown to 4.1 trillion dollars in value before falling back in the wake of the financial crisis in 2008. At the height of the IT-bubble takeover boom of 2000, takeovers reached previous heights of 3.8 trillion dollars in value. Davidoff finds that the number of deals went the same way, growing from 20 000 deals in 2004 to 46 000

[1] Previous takeover waves broadly refer to the *first* (1893-1904), *second* (1919-1929), *third* (1969- 1973), *fourth* (1984-1989) and the *fifth* (1993-2000). The *sixth* began in 2004 and ended with the global financial crisis 2008, when Lehman Brothers crashed in September that year.

deals in 2007. This dissertation addresses a sub section of this takeover market, *cross-border hostile takeovers*. Specifically it deals with cross-border hostile takeover *processes*, the theoretical rationale behind the political pursuit to enable it, the process governing the outcome, the development of regulation to enhance the process and how all this relates to the value-creating process of the corporation.

Studying these processes from both a theoretical and empirical view I believe to be relevant for a number of reasons. Despite the fact that there remain few cross-border hostile takeovers (since hostile bids make up only a few per cent of the deals – even in shareholder friendly markets such as the British one) – those that do emerge are often high profile, *very* public and heavily debated among politicians and in local communities. Cross-border hostile bids also influence actors on the market for corporate control more generally. Cross-border hostile takeovers encompass both the idea of the corporation as a value accretive entity for society at large and the idea of an efficient market of corporate control built on financial theory. Understanding the social process of a cross-border hostile bid contributes to the development of the to date quite novel research field of comparative corporate governance (Aguilera & Jackson, 2003).

During the sixth takeover wave hostile bids were more common than during previous merger waves. Proxy-organization *Riskmetrics* gives an indication of this hostility in a report on activities by institutional investors, showing that proxy fights in the US grew from 30 to 41 in 2008, a growth of 33 per cent, and continued to soar above 50 as of June, 2009 (Young, 2009). During the sixth takeover wave Europe also came to play a new and intensified role in this cross-border battle for control. Broadly speaking, a pan-European cross-border hostile takeover market dates back to 2000, during the height of the *fifth takeover wave*. This was marked by the successful $199 billion (GBP 132 billion) cross-border hostile bid by British mobile phone group Vodafone for German Mannesmann in 2000, at the time the largest cross-border deal ever to take place in Europe.[2] During the sixth takeover wave the cross-border hostile-bid fights continued. High profile examples include activist funds' TCI and Atticus joint attack on Deutsche Borse in 2005 after Deutsche Borse had bid on British LSE. Other examples include TCI and Centaurus' joint attack on British-Indian steel company Mittal Steel in 2006, after Mittal had bid for French Arcelor to form the world's largest steel-company, a well as Standard Life's protests in 2006 over Indian Tata Steel's bid on Corus, as well as Ethos and Swiss SS Funds' joint attack in 2007 on GIC of Singapore's bid on the Swiss investment bank UBS (Young, 2008, 2009). Incidents of direct political engagement were few but French President Jacques Chirac's criticized plans from US-Pepsico to bid for French yogurt producer Danone in 2005. Thereafter the French government came up with eleven strategic commercial sectors that should be protected from foreign takeovers (Franks, BBC 2006). In April 2005, the German SPD politician Franz Münterfering attacked hedge-fund activities on the Frankfurt Stock Exchange calling the funds "grasshoppers" *(Gr:* "Heuschrecken").

The Nordic country of Sweden was no exception. The Swedish market for corporate control since the 1990s has been second only to UK (see e.g. Tson-Söderström, 2003) and during the sixth takeover wave activities increased. The country experienced delicate cross-border bid-fights such as South African-British Old Mutual's bid on the insurance company Skandia in 2005 and the German vehicle conglomerate MAN and Volkswagen's hostile takeover fight for Scania 2006-2010 that was still not fully settled in 2012.[3]

Seen as a group, these cross-border hostile deals were partly the result of a changed political landscape. In the 1990s the European Commission set out to enhance European growth opportunities and

[2] It was followed by hostile takeovers in Italy (Olivetti for Telecom Italia; Generali for INA) and in France (BNP Paribas; Elf Aquitaine for Total Fina), but these are made up of coalitions of domestic players.

[3] Among early high-profile cross-border deals were the planned merger between vehicle companies French Renault and Swedish Volvo (1993) and the merger between pharmaceutical companies Astra and Zeneca (1999).

strengthen European global competitiveness vis-a-vis the US and Asia. It was believed that one way to reach this was to increase the efficiency of the market for corporate control through creating a *level playing field* among corporate actors. One cornerstone, among other activities, was the work with the *13th Company Law Directive on Takeovers* aimed to facilitate cross-border takeovers, including hostile takeovers.[4] The work was facilitated by the deregulation of previously captive financial markets during the 1980s and 1990s and a focus on enhancing liquidity on capital markets with the overreaching political aim to increase efficiency, all in accordance with modern financial theory and the predominant belief at the time in the *efficient market theory*. This work was enhanced by the parallel growth of a savings industry with pension and mutual funds investing in listed companies across Europe.[5] During the same period the *shareholder-value model* of corporate governance, an Anglo-American development, became the preferred norm throughout Europe, leaving stakeholder-governance ideas behind (see e.g. Aglietta & Reberioux, 2005, for a discussion on shareholder value and the quest for leverage). National takeover regulations both developed and were revised a number of times. It was a period commonly referred to as *financial capitalism.*

The global financial crash of 2008 and the subsequent economic downturn cooled off activity on the European market for corporate control. However, hostile cross-border takeover fights still received public attention. In the autumn of 2009 the UK, the most liberal of the European market economies, experienced its own high profile and delicate cross-border hostile takeover. This time it involved the US-based food and beverage company Kraft bidding for British Cadbury, famous for its chocolate. By the time the deal was closed, in early 2010, it had revealed

[4] Among readings from the *Commission* a good start is the Winter report; "Modernising Company Law and Enhancing Corporate Governance in the European Union – A Plan to Move Forward", Commission of the European Communities, Brussels, 21/5, 2003.

[5] The liberalization of financial markets began with president Ronald Reagan in the US and premier minister Margaret Thatcher in the UK during the 1980s and slowly spread across countries. Sweden opened up for foreign free investment on the stock market in 1990.

UK-public concern over both *short-termism* among institutional investors and *regulatory arbitrage* among actors due to different regimes of corporate governance and takeover regulation in the UK and US.[6] The US-UK Kraft-Cadbury battle exhibited familiar traits experienced in Swedish cross-border fights during the sixth takeover wave.[7]

Davidoff (2009) writes that the sixth takeover wave seemed to differ from its predecessors in three respects: the mergers were bigger in size, many were cross-border takeovers and investment banks played an important role in the success of the bids. Also, hostile takeovers and shareholder hostility towards incumbent boards of directors grew to unprecedented heights.

Thus, at the height of the sixth takeover wave and in its aftermath the activities around cross-border hostile takeovers were ripe for scrutiny by politicians and regulatory bodies across Europe. This involved reassessing the role of the EU in the regulatory development of a market for cross-border hostile takeovers, including questioning how successful EU had been in its work to converge differing regulatory regimes. In a revision of the UK takeover regulations in 2011, the position of the target board during a bid-fight was strengthened. In 2012, a UK government commissioned independent review on "long-termism" called for the government to more actively question the ease of which foreign companies

[6] In December 2009 the Financial Times wrote that Lord Mandelson, Britain's Business and Enterprise Secretary, had warned the board and management of Kraft and was quoted as saying: "If you think that you can come here and make a fast buck you will find that you face huge opposition from the local population . . . and from the British government." (Guthrie & Wiggins, FT, 12 May 2009). The UK secretary's comment was unprecedented, marking a government intervention previously unheard of in a country where politicians tend to steer clear of becoming involved in takeover bids unless there are serious competition concerns. In the UK House of Commons in March 2010 there were calls for a "Cadbury Law to prevent hostile takeovers of British companies which are not in the public interest" (Wiggings, FT, 12 March 2010).

[7] It will be shown later in the text that Sweden in many sense is much more shareholder-friendly than the UK, as the shareholders fully control the process for recommending board of directors; each director is elected for one year-terms, and often the CEO is not a member of the board.

could buy UK listed companies, and proposing that the UK government more actively questioned claims of benefits from large corporate transactions, including weighing in effects on employment in the UK, long-term financial strength of the merged entity and the future for high level functions (Kay, 2012).

Sweden also felt it necessary to revise its regulations, in 2009, forming the last NBK Takeover Rules. However, this revision and its update in 2012 did little to address the role of the target board in relation to the target corporation. Rather, the revisions appeared to be focused on further facilitating takeovers (i.e. liquidity) and further enhancing the current shareholder focus of the board (i.e. short-termism). Understanding the divergence between financial theory of a market for corporate control and the regulatory development of cross-border (hostile) takeovers constitutes a central theme of my dissertation.

1.2 Personal interest in the topic

In the autumn of 2006 I was offered to conduct an in-depth study of Old Mutual's hostile bid on Skandia 2005, together with Assistant Professor Markus Kallifatides and Professor Sven-Erik Sjöstrand, Department of Management and Organization at SSE. Authored by Kallifatides et al. (2010), the book *Corporate governance in modern financial capitalism, Old Mutual's hostile takeover of Skandia*, reveals a cross-border hostile takeover that featured both regulatory arbitrage and short-termism among institutional investors. This deal involved regulatory arbitrage between different systems of corporate governance – one UK based, one Swedish based but also from South Africa and the US. It involved the Swedish model of shareholder involvement through the nomination committee (in the Swedish code of corporate governance), a system that enables a group of the largest shareholders to come together to suggest directors to be elected at the AGM. In Skandia, institutional investors both participated on the nomination committee and held private talks on strategy with the chairman and the directors. It also involved the forced merger rule (in the Companies Act and rewritten in 2007), stock-market announcements and the role of investment banks during a takeover (Swedish takeover regulation and rewritten in 2009), insurance regulations (Insurance Companies Act and rewritten in 2007) and the law on insider trading (Insider Penal Act and Market Abuse Penal Act). It also featured short-termism among shareholders where mainly institutional investors followed a financial rationale and sold off shares for index-tracking reasons rather than corporate and operational reasons. In the Swedish legal environment with corporate governance applied to a listed company with a dispersed ownership structure, this could easily be detrimental to such a company's survival as an independent entity. The fight revealed an apparent uneven power play between short-term oriented institutional investors and the board of directors, where some of the persons involved found it difficult to tackle the different, and sometimes contradictory, obligations presented in the takeover regulation targeting different shareholder groups and the Companies Act. Thus, the Skandia-deal appears to have been embedded in its historical, social, regulatory and cultural context where Sweden's transformation from industrial to financial capitalism and opening up of previously captive capital markets played a part (Kallifatides, Nachemson-Ekwall & Sjöstrand, 2010).

Another cross-border hostile takeover that I studied as part of this dissertation is the German commercial vehicle companies MAN's and Volkswagen's bids, in different turns, on Swedish Scania. Whereas the Skandia-deal can problematize the issue of a dispersed shareholdership and the Swedish governance model with its openness to shareholder involvement, the Scania-deal can be approached as being embedded in the historical Swedish governance context of controlling shareholders and stocks with differing voting power. This latter deal involved regulatory arbitrage between German and Swedish based governance procedures.[8] The deal also involved regulatory arbitrage as actors arbitraged between the Swedish culture of a blockholder setting and the 30-percent mandatory bid-rule (with a Swedish local adoption of an EU directive). It is also

[8] There are plenty of articles from 2006 written by Nachemson-Ekwall, S. This will also be developed in one of the case studies.

fair to say that the Scania-deal revealed how the rationalities of financial capitalism, shareholder-value governance and the tendency of short-termism among institutional investors influenced the behaviour of controlling blockholders in both countries.

With this in mind I began to doubt whether many cross-border hostile takeovers during the sixth takeover wave were the result of the creation of a so-called "efficient market for corporate control", in line with a standard textbook utility-maximizing neoclassical economic model of rational actors.[9] Maybe the success of these hostile bids was the result of something else? Many of these cross-border hostile takeovers seemed to reflect a new power dynamic between actors on the financial market. In line with Davidoff (2009) the masters of this power play were found among investment banks, but also among institutional investors, such as activist shareholders that took the role of catalysts for change and, in that position, received support from institutional investors such as traditional pension funds. Also, in contests for corporate control, shareholder value seemed to have become a buzzword on capital markets and through this enhancing short-termism as opposed to long-term value creation (Aglietta & Rebérioux, 2005). In this dissertation I wish to clarify if the outcome of cross-border hostile takeovers during the sixth takeover wave reflected a well functioning capital market with utility-maximizing actors or if the outcome reflected a changing domestic institutional context related to local laws and regulations that some actors were better equipped to exploit than others.

1.3 Objective

The creation of a (theoretically) efficient market for corporate control by *levelling the playing field* among corporate actors and enabling cross-border

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[9] The efficient market theory requires agents to have rational expectations implying that agent's expectations of future economic outcome cannot be systemically wrong in the sense that over time the random and statistical outcome will reflect average expectations.

hostile takeovers is often seen as one of the most powerful corporate governance mechanism available (Manne, 1965). This quest for a perfect capital market is intimately linked to an Anglo-American and Berle and Means (1932/1968) shareholder-value perspective on corporate governance where the threat of a hostile bid assures that management work to enhance value for shareholders (as advocated by Jensen & Ruback, 1983). This includes the emergence of a dispersed shareholder-owner structure and corporate governance in the hands of the board and management. The presence of controlling large family owners and protective regulatory devices in Europe have been well described in the *Varieties of capitalism literature* (Shleifer & Vishny, 1997; Hall & Soskice, 2001; Becht, Bolton & Röell, 2002; Gourevitch & Shinn, 2005) as well as expected regulatory convergence towards the Anglo-American model of governance (Hansmann & Kraakman, 2004).

During financial capitalism, the European Commission appeared to have plenty of arguments set out in support of tearing down protective devices and streamlining of national governance devices. However, the public and politicians were not alone in their scepticism towards how this level playing field came to work in the Europe during the sixth takeover wave. It was not that mergers and acquisitions were questioned per se, a well functioning market for corporate control has merit and there are plenty of successful examples, but as stated previously there was a growing scepticism towards how the mechanism had become to be used during cross-border hostile takeover-fights. The idea of the hostile bid also received criticism from academia, claiming it to be either a rather blunt mechanism for corporate restructuring (Berglöf & Burkart, 2003; Gilson, 2005) or not working as expected on deregulated capital markets with active institutional investors (Aglietta & Reberioux, 2005; Wymeersch, 2008). Van Apeldoorn and Horn (2007) claim that the EU's ambition to create a vital cross-border market for corporate control clashes with national regulations, domestic protective measures and local sentiment. In addition, a regulatory focus on (cross-border) hostile takeovers might be too simplistic a governance instrument as it dismisses institutional differences among organizations, including path dependency and social, cultural and historical embeddedness (Granovetter, 1985; Fligstein, 2001; Roe, 2003; Aoki, 2003, 2007; Jackson & Miyjami, 2007).

Broadening the perspective in this dissertation, I take a closer look on the idea of a market for corporate control, contingent on finance theory and the theory of efficient capital markets. In a quest to understand the implication this has had for the regulatory works on the creation of a (pan-European) market for cross-border hostile takeovers I present a complementary theory developed from the perspective of the corporation as a value accretive entity and adding to sociology and historical institutionalism. This will answer the call from Aguilera and Jackson (2003) for an actor-centred institutional approach to governance that integrates simultaneous social processes of continuity and change across boundaries of different governance models and adds to the understanding of the effects of regulatory changes across borders. Thus I approach the question of the market for corporate control from three perspectives:

- I draw on finance theory of the market for corporate control and add notions such as regulatory convergence, social embeddedness and path dependency in corporate governance to bring in a more dynamic institutional perspective.

- I explore the ideas behind the creation of an efficient market for corporate control in relation to cross-border hostile takeover processes involving Swedish targets.

- Last, I describe in what way the 2009 revision of the Swedish takeover rules theoretically addressed problems related to both the creation of an efficient market for corporate control and to the corporation as value accretive entity.

This will be done by presenting empirical material from six studies involving a) two descriptive studies of the institutional setting in Sweden with its particular shareholder friendly governance regime, very active takeover market and evolving takeover regulations, b) three case studies, presented as narratives, of cross-border hostile bid processes from the sixth takeover wave and finally, c) an analysis of Swedish takeover rules as they came to work during the sixth takeover wave and the revision of them in 2009. This is then compared to the institutional settings of the UK, USA, Germany as well as the EU with a focus on the 13^{th} Directive on takeovers. The cases are Old Mutual's hostile bid on Skandia 2005 (Kallifatides, Nachemson-Ekwall & Sjöstrand, 2010), the private equity bid for Capio 2006 (Nachemson-Ekwall, 2012b, unpublished manuscript) and VW's and MAN's takeover fight over Scania 1997-2011 (Nachemson-Ekwall, 2012c, unpublished manuscript).

My starting point is to look at companies with a dispersed-shareholder structure (Skandia and Capio) and from that perspective move to a target company with a focused, controlling-shareholder structure (Scania). The first deal emanated from a bidding actor in a country with strong tradition of self-regulation and soft law (the UK). The second deal involves private equity as the bidding actors were incorporated in tax havens and controlled through a governance-model that differs from a listed Swedish company, as such featuring a setting similar to a cross-border bid situation. The third deal involves two bidding actors from a rule-based stakeholder setting (Germany). I will try to show how the evolving conflict between actors (always present in a hostile situation) relate to the Swedish shareholder-oriented model of corporate governance, possible short-termism among institutional investors and regulatory as well as moral arbitrage by actors from different national governance systems.

I am also interested in finding out in *what way* and to *what extent* the 2009 revision of the Swedish takeover rules solved the problems detected in the case studies related to a cross-border fight involving a Swedish target. In particular, I aim to draw attention to the 2009 enhancements of deal making and strengthening of the shareholder focus of Swedish takeover regulations that were further enhanced in the revision 2012. The analysis relates to two of the main building blocks of European takeover regulations – the role of the target board and the *Board Neutrality Rule* as well as the quest for equal treatment of shareholders and the *Mandatory Bid Rule*. Both rules were addressed in the 2009 revision of the Swedish takeover rules. I then use a description of capital market regulation to highlight regulatory and moral arbitrage by actors leveraging on differences in national corporate governance regimes.

Using the perspective of the board of directors, in their role as fiduciaries of the corporation, I will try to show how some of the amendments to the Swedish takeover rules 2009 increased the focus on the rights of shareholders as compared to those of other shareholders, current as well as future, as well as other stakeholders. I will call into question whether this has been done in such a way that, in an investor-environment of financial capitalism dominated by institutional investors, this might represent a deviation from both the theory of the firm and company law, possibly weakening the board's ability to act for a company's long-term value creation. On this basis I have formulated my research question as:

> "How can we understand the idea of a well functioning market for corporate control and the effects of regulatory convergence of different corporate governance regimes (in Europe) in financial capitalism?"

The study of a phenomenon will hardly leave one clear answer. Rather, my research question will result in a set of hypothesis, and from these further theory can be developed.

1.4 Contributions

I believe this dissertation to contribute to our understanding of the theoretical concepts of a well functioning efficient market for corporate control and the effects of regulatory convergence of different corporate-governance regimes (in Europe) in a setting of financial capitalism. This includes the application of European and British takeover rules to a national governance regime, which has moved from a stakeholder focus to a shareholder focus while at the same time encompassing companies with both controlling shareholder structure and companies with dispersed shareholder structure.

The existing research involving takeovers has mainly been conducted within different academic disciplines – addressing takeover regulation from a pure regulatory and legal perspective, presenting quantitative studies of the takeover market grounded in the field of finance, or focusing on either the pre-phase or post-phase of the takeover.

There are a few Swedish case studies of power struggles on the market for corporate control. One such study is a struggle for control in the pulp and paper industry (Ericson, 1991; Sjöstrand, 1997). The parties involved were Stora and Modo, two globally integrated pulp, paper and packaging companies from different Swedish banking spheres, when they competed in the early 1980s for the packaging company Iggesund. The study illustrated different rationalities of the actors in a takeover process, but as this took place when Sweden still had currency regulation it only involved Swedish actors. Other studies of hostile takeover process are more anecdotal: such as Sundqvist's (1994) account of French state-owned Renault's attempt to merge with the Swedish vehicle company Volvo in 1993. This was one of the first cross-border deals in Europe, but also this case only involved Swedish shareholders.

A second category of studies has taken the perspective of the capital market and shareholders (examples of this are Bjuggren, Eklund & Wiberg, 2007; Jonnergård & Larsson, 2008). Bengtsson (2005) uses institutional sociology to study how Swedish institutional investors engage in shareholder activism in portfolio corporations.

A third category of studies focuses on the high propensity for takeovers on the Swedish Stock Exchange. Henrekson and Jakobsson (2003) claim the lack of Swedish owners to reflect a historical tax-system disfavouring private capital formation on the one hand and favouring the collectivisation of savings and pension plans on the other hand. Burkart and Lee (2007) conclude that the Swedish governance model with multiple voting rights through A and B shares[10] does not hinder takeovers and as such shall not be viewed as a protectionist device hindering corporate restructuring-processes.

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[10] The Swedish usage denotes the A shares the power of one vote and the B-shares the power of a tenth of votes.

A fourth group of studies instead address the post-takeover period and the integration process. Borglund (2006) describes four case studies of the implementation of the shareholder-value rationality on Swedish targets, previously embedded in the "Swedish-stakeholder model". Holtström (2008) focuses on the ability to realize synergies after a merger of two Swedish companies. Henrekson and Jakobsson (2012) extend the owner discussion by including the Swedish corporate governance model as a factor explaining the diminishing role of Swedish owners and lack of companies listed on the Swedish stock exchange.

This dissertation extends on the above Swedish studies through discussing the actual takeover *process* in more detail. In doing this it includes the perspective of the corporation as value accretive entity and describes how Swedish shareholder governance and regulations of takeovers have been put to practise in financial capitalism. Moreover, none of the above studies bring into question the actual idea of an efficient market for corporate control. The term "efficient" is related to mainstream finance theory, and end with reasoning that a market that enables hostile takeover activity is valuable *per se*. If instead the "efficient"-term is broadened to encompass more perspectives (such as being efficient for whom, where and in relation to what?) institutional theory is added to the discussion. This broader perspective allows for an eclectic research tradition where a selection of concepts from the fields of management, economics and law are included. By drawing on Aguilera and Jackson's (2003) actor-centred institutional approach to governance, I show that integrating simultaneous social processes of continuity and change across boundaries will further our understanding of how national governance models develop, and why some regulatory changes have not generated the expected outcome (i.e. a financially efficient market for corporate control). I show that it is not only the case that convergence does not emerge but the generated outcome might be something all together different and unexpected, reflecting the social process whereby actors or coalitions of actors take advantage of the situation when the previous model is destabilized. I also draw on the idea by Aguilera, Filatotchev, Gospel and Jackson (2007) of including *costs, contingencies and complementarities* into the analyses. This approach broadens the analytical perspective to include how interdependencies between the organization and diverse environments lead to variations in the effectiveness of different governance practises.

The dissertation will hopefully contribute to future development of regulatory work promoting integrated financial markets in the sense that this work might encourage regulators to include more perspectives than only assumptions emanating from mainstream finance, ideas of efficient capital markets and the concept of rational actors. This opens for a focus on the role of the corporation during a cross-border hostile takeover process. A discussion of Sweden's experience in financial capitalism, this country's move from stakeholder-value governance to a particular form of shareholder-value governance, and this country's active market for corporate control can also be used to further understand what is going on in other markets. For practitioners in Europe and the UK, addressing both policyholders and market actors, the case of Sweden could be useful knowledge in the continuing work to develop a sustainable pan-European corporate governance and takeover framework.

1.5 Limitations

This dissertation studies a social process in which certain behaviour is reinforced by the reaction of others. It draws from finance, economics, management and law. This might be considered a theoretical weakness but I would rather view it as strength. At least it is fair to say that an open mind is a prerequisite for understanding social processes and institutional change.

As the empirical setting I limit my study to Sweden, its governance-regime, takeover rules and culture. The empirical time period is the era of financial capitalism, which means that actors and contexts are related to actions on the capital markets during a period from the 1980s and forward. Within this setting I foreground three clinical longitudinal case studies of cross-border hostile takeovers of Swedish listed company. The first is a cross-border hostile takeover of a company with a dispersed shareholder structure, Skandia. I focus mainly on the position and role of the board of directors of the target company (i.e. Skandia) in relation to its shareholders rather than the question of equal treatment between different groups of shareholders. I also limit my discussion of the board of directors of the bidding company (i.e. Old Mutual) to its activities relating to the target-company and shareholders, leaving aside the bidding company's relationship to its own constituents, including its shareholder-owners.[11] The Skandia study can be seen as a version of the agency problem addressed in the EU Takeover directive's Board Neutrality Rule.

The Skandia study is then related to a smaller clinical study of a company also featuring a dispersed shareholder structure, Capio. This is used to give perspective on the findings in the Skandia case related to the 2009 revision of the NBK takeover rules. In the Capio study, this will mainly relate to two problems: transactions involving parties working in coalition without public knowledge, so-called *Concert Party Transactions* and directors' loyalty.

After this I broaden the perspective with the inclusion of a third study involving a cross-border hostile takeover of a company with a classic controlling blockholder shareholder structure, Scania: this time involving bidding parties from a very different governance regime. However, given the delicate development of the cross-border hostile fight involving both German Volkswagen and MAN as bidding parties, I focus on the relationship between a controlling shareholder and minority shareholders and how this develops during a cross-border hostile fight between actors complying to different corporate governance systems. These are the German corporatist stakeholder-model and the Swedish shareholder model of governance. In the perspective of the EU Directive and takeover rules the Scania–VW–MAN case mainly revolves around the agency-conflict between different shareholder groups, addressed through the Mandatory Bid Rule.

I also include a fourth case study, evolving around a critical analysis of the Swedish Takeover rules in place in 2003 and the 2009 amendments to the Swedish Takeover rules, the NBK rules, to those amend-

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[11] This is for logistical reasons as many of Old Mutual's shareholders were based in South Africa.

ments to these rules most relevant to the Skandia, Capio and Scania cases. This case study omits detailed aspects of the takeover market such as prospectus writing, legal defence tactics by the board as well as related regulations addressing transparency and general shareholders rights that have also been of concern of regulators. Rather, the focus is on the position and role of directors, in the Skandia and Capio cases, and the implication of regulatory arbitrage in the case of Scania. This approach to takeover regulation has two limitations. The first is that the study, while dealing with a legal matter, does not analyse the amendments to the takeover rules from a strictly legal perspective. Instead I integrate economics, sociology and management into the discussion. The second limitation is that I have not made an in-depth study of the actual process of developing new takeover regulations itself. I have only used public documents. I also limit my study through using the EU Takeover Directive and the UK Takeover Code as point of reference, especially the latter since it has been used as a model for Europe and Sweden. I also draw on open sources from the US and German takeover markets. As mentioned above, I especially focus on the two of the building blocks of the Directive – the Board Neutrality Rule and the Mandatory Bid Rule. In Skandia and Capio the empirical parts cover the timespan 2004–2006. In Scania the perspective is broader, starting in 1996 with the fight still not yet settled in the autumn of 2011.

1.6 Organization of the thesis

This dissertation proceeds as follows:

Chapter 2 includes a theoretical frame of reference, describing the relevant concepts; institutional theory, the theory of the firm, value creation and corporate governance, financial capitalism and the ideas behind the creation of an efficient market for corporate control.

Chapter 3 develops the theoretical drivers for a market for corporate control including a discussion of the focus on shareholder value, agency theory and regulatory quest for liquid capital markets.

Chapter 4 constitutes the methodological chapter. It presents my epistemological perspective and the six studies of which four are case studies.

Chapter 5 is the first of the six studies and describes the institutional setting for the Swedish market for corporate control in relation to the Swedish model of corporate governance. This is compared to the Anglo-American and the German contexts.

Chapter 6 is the second study and includes an historical description of the Swedish takeover market and takeover rules. Just like in the first study these are compared to the Anglo-American and German contexts.

Chapter 7 turns to the sixth takeover wave. This part includes both a presentation of the three empirical case studies Skandia, Capio and Scania and a summary of the main findings.

Chapter 8 constitutes the sixth and last study. It deals with the amendments to the Swedish takeover rules between 2003 and 2009. It includes a description of the shareholder orientation and an analysis of the amendments compared to regulations in the UK, the US, Germany and also the Takeover Directive.

In *Chapter 9* and the last chapter, *Discussion and Results*, I analyse how successful takeover rules have been in dealing with the original problem as defined by the Commission, of levelling the playing field among European corporate actors. Building on institutional theory I draw conclusions related to the original ideas governing the creation of an efficient market for corporate control. I end with a discussion of the policy implications of my findings.

Chapter 2

Theoretical frame of reference

2.1 Purpose and structure of this chapter

The purpose of this chapter is to introduce the basic concepts of the framework that has shaped a market for corporate control that enables cross-border hostile takeovers. This framework will be used as a reference to the theoretical drivers for a market for corporate control (in Europe) described in more detail in Ch. 3.

I begin with using institutional theory, which introduces sociological, organizational and dynamic processes into the market for corporate control. A cornerstone in any sociological analysis is the view that the human being is far from a rational actor always ready to optimize decisions to maximize his/hers economic value. Here the human being is rationally both complex and bounded in his/her decision-making. I use this description of human beings to theoretically conceptualize the interaction between actors and organisations that form the arena for cross-border hostile takeover processes.

Three main theoretical concepts are used to conceptualize this complex institutional organizing of cross-border hostile takeovers. The first concept is the firm or the *limited liability company* (Ltd), without which there could not exist a market for corporate control. How this entity, the firm, is governed to enhance a value accretive process is then discussed from an organizational perspective. In this context I also include a description of different models of corporate governance, the stakeholder model and the shareholder model. As a second concept, I use mainstream finance theory. The *efficient market hypothesis* has been a dominant research path of academics working with corporate finance and capital markets ever since the 1980s. Finance theory has shaped the development of today's liberal market capitalism and its capital market regulations, both necessary components for a cross-border hostile takeover market to emerge. The efficient market hypothesis has not passed without criticism, as it simplifies human rationality and decision-making. My third theoretical concept is the efficient market for corporate control. This theory links value creation of the limited company with financial economics and ideas about "efficient" capital markets, where prevalence of hostile takeovers is seen as proof of the existence of such a market.

The chapter ends with a recount of the theory of hostile takeovers where the market for corporate control is seen as a market where different management teams compete for control in the interest of society at large. This competition is complicated by the question of the distribution of price-premia, to be equally distributed among all shareholders alike or to those that have the strongest bargaining power. Manne (1965) claims the premium to belong to the individual shareholders and as such legitimize differing price offers whereas Berle and Means (1932) claim the premium to belong to the company, to be distributed equally among target shareholders. Thus, contradictory goals are embedded already in the theory of the market for corporate control. This complicates the role regulators play as facilitators of a market for cross-border hostile takeovers.

2.2 An institutional perspective

Institutionalism emerged as an academic field with roots in American socioeconomic thinking at the turn of the 20th century.[12] Institutionalism views markets as a result of a complex interaction of various institutions; a coherent systems of norms manifested in mental maps, norms or physical arrangements. Here an institution is usually linked to lengthy historical trends or dominating cultures (Sjöstrand, 1995, 2005), i.e. it is a social process. Human action plays an important role in any social process and the bounded multi-rational individual moves markets away from the three classical assumptions of economics that usually are referred to in textbooks; that people have rational preferences among outcomes; that individuals maximize utility and firms maximize profits; and that people act independently and on the basis of full and (over time systematically) relevant information. It is not so that the assumptions are viewed as wrong per se. They function as tool for building mathematical models. However, as a reflection of reality the classic model of economics needs to be adjusted in a number of ways and this appears to have brought with it a number of complications that sociology addresses. Building on institutional theory, human activity is instead influenced by a number of ideas, relationships and traditions, which together make human decision-making multifaceted and complex.[13]

This view also relates to the influential works of Simon (1957) and his conceptualising of the organization where individuals have limited decision-making capability (i.e. *bounded rationality*) and where decisions are taken on limited or available information (i.e. *satisficing*). Simon argues that it can be viewed as rational to seek to satisfice in that the process of

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[12] For a discussion of institutionalism see Powell and Maggio (1991), Scott (2001) and Academy of Management Journal (2002).

[13] Sjöstrand (1997) offers a detailed account of how the ideal manager to succeed combines both rational and irrational approach to leadership. This complexity of human decision-making can be described as forming a homo complexicus nature very different from the classic construct in the model in 20th Century Economics. See also the methodological section of this dissertation.

looking for better solutions/results expends resources. A better solution would have to justify the extra costs carried in finding it. Simon's critique on the utility maximizing man builds on four principles (Sjöstrand, 1985: p. 69):

- Consumers do not maximize (subjective) utility. That is shown in numerous experiments.
- (Profit) maximization does not work as a guide for decision-making in companies.
- The concept of rationality means something different in the absence of perfect competition.
- Making predictions is a complex multi-rational process.

Thus, the power and decision-making within an organizational system might not reflect an economic rational or utility maximizing activity but rather the optimal decision given the situation.

The institutional perspective used here also bears traces of Berger and Luckman (1966), that claim that, inspite of their apparently objective existence, institutions are in fact the result of a long social (re)-production process. This is why institutions cannot be understood without studying the historical process from which they have developed. Thus, a current institutional setting is never the final solution; it is a temporary result of social embeddedness (Granovetter, 1973) and path dependency (Davies, 1985). Path dependency is here a term for contingent, non-reversible, dynamical processes. Markets for corporate control are then social constructions – institutional arrangements – that have developed through the interplay of actors over time.

On the macro level ideas of bounded rationality, social construction and path dependency have implications for the introduction of new ideas into a society. Here I relate this macro perspective to the concept of space and regulatory space as described by Crouch (1986; referred to in Hancher & Moran, 1989, pp. 271–299), and also developed in Scott (2001) to build an analytical construct that addresses interdependencies between different agencies. Because it is a space it can be allocated among several actors, but it is also available for occupation. Bargaining power varies across interest groups as do the possibility of regulatory capture. Notably Hancher and Moran (1989) claim that this bargaining is embedded in democratic systems, through which parliamentarism epitomizes the very idea of regulatory capture (from lobbyist groups) and bargaining (between parties of various strength).

Hancher and Moran (1986) add different specifying concepts to the more general notion of regulatory space, such as historical timing, organizational structure and interdependencies. They claim that allocations of power within regulatory spaces are influenced both by legal tradition and by a wide range of social, economic and cultural factors.

Institutional economic theory tends to highlight the existence in all particular nations in the European union of pre-capitalist actors, elites, labour unions, corporations and their associations, political parties, embedded in various kinds of structures, demographic, economic and cultural (i.e. Polanyi, 1944; Granovetter, 1985; Sjöstrand, 1993; Whitley, 1999; Hall & Soskice, 2001; Fligstein, 2001; Aguilera & Jackson, 2003; Roe, 2003). In what way these different actors have influenced the development of a pan-European market for corporate control and cross-border hostile takeovers will be elaborated on in Ch. 5 and Ch. 6.

2.3 Concept 1: Corporation and governance

2.3.1 Theory of the firm

The first concept of the complex institutional organizing of cross-border hostile takeovers is the entity of *the firm*, including the question of *value creation* and different systems of *governance*. In this section this will be approached in three separate subsections. Starting off with the corporation, the *limited (liability) company* is a product of legal rules, regulations and norms (Micklethwait & Wooldridge, 2005; Nerep & Samuelsson, 2009). The goal of the limited company is to increase risk-taking in society through the separation of financial responsibility from the individual persons by transferring it to a company. The overreaching belief is that this is beneficial and value accretive for society at large. A popular way to describe this relationship between jurisprudence and value creation is the idea that a limited liability company must deliver value to legitimate its existence, often described as a ”license to operate”.[14] The actual construction of a limited company is an organization with boundaries that lock in capital such as equity and bonds to enable value creation in the interest of society. Those providing the most risky capital to enable this process, shareholders, must somehow be compensated and are compensated last as *residual claimants*; that is when all other parties involved in the company (such as employees, customers, the government in the form of taxes) have received their stake. This compensation to shareholders, in the form of dividend, can be delivered in two different ways – either immediately (short-term) when the generated profit from the value accretive activity is distributed immediately, or in the future (long-term). The profit (residual claim) can be reinvested in part or in full in the corporation's activity to enable corporate value to grow and deliver future dividend.[15]

Shareholders appoint a board of directors that is responsible for setting the company's agenda and for monitoring management during the year. The board is responsible for enrolling the CEO and sometimes part of the management team and for implementing an organizational process able to support the allocation of resources for (long-term) corporate value creation. However, this structural set-up with a separation of ownership and controlling executive does not go without complications. As early as the 18th century Adam Smith noted that single shareholders in a company with numerous owners each posses limited influence over management decisions.

[14] OECD leans towards this definition, which has also influenced IFC and the World Bank in their view on corporate governance and social responsibility.

[15] For example, the Swedish Companies Act, 3 Ch. 3 §, states that the purpose of the company is to generate profit for the shareholders, but it does not state how much profit.

In a classic text *On the Wealth of Nations*, Smith (1776) states that:

> 'The directors of such companies… being the managers rather of other people's money than of their own, it cannot well be expected that they should watch over it with the same anxious vigilance with which the partners in a private co-partnery frequently watch over their own. Like the stewards of a rich man, they are apt to consider attention to small matters as not for their master's honour, and very easily give themselves a dispensation from having it. Negligence and profusion, therefore must always prevail, more or less, in the management of the affairs of such a company. It is upon this account that joint stock companies for foreign trade have seldom been able to maintain the competition against private adventurers. (Book 5, Ch. 1, part 3:1).

Modern interest in the separation of ownership and control is often associated with Berle and Means (1932) who documented the rise of the modern corporation in the United States. Here the separation of power between owners and management was a product of the emergence of large corporations, as that diluted shareholders' control and transferred power to management, which in a US historical context was more or less the same as the board. However, it took until the 1960s for the Berle and Means-firm, with its dispersed shareholders and managerial control, to emerge as the standard form of control and governance of a US listed company.

Coase (1937) explained why there were firms and not only markets, the firm itself being a closed trading system, claiming that there were to be (transaction) costs connected to the use of the "price mechanism". Coase claimed that it sometimes was cost-efficient to organise part of the production resources within defined and closed boundaries.

Coase's construct of the firm is basically a hierarchical one, through which the governance function has been differentiated in such a way that the act of ownership and the operational management has been allocated to different actors. This division of functions of the corporation has not only enabled risk-taking but also a growth in size, acquisitions, the emergence of company groups of companies and large global enterprises.

Alchian and Demsetz (1972) built on Coase's theory of the firm when they explored different ways to organize production effectively.

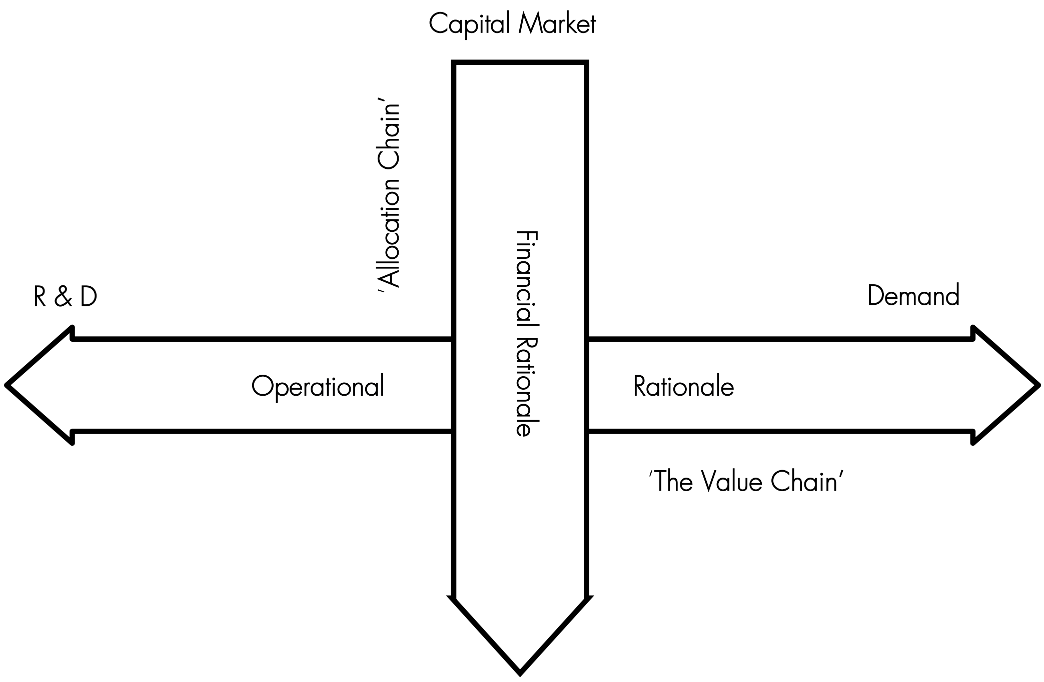
Whereas Coase's theory built on one sole businessman owner – the entrepreneur – Alchian and Demsetz transformed the monitoring of the firm's production to a setting with multiple corporate owners. As such, it was seen as run by a manager separated from the multiple shareholders. Costs related to the monitoring included bureaucratic inconveniences in paying individual shareholders the cost of monitoring, costs related to the risk of shirking by shareholders and moral hazard. Equally troublesome was the risk that a sole shareholder-actor made bad decisions when the cost was distributed to all other investors. Alchian and Demsetz contractual idea transformed the Coasean firm into something that continuously could be monitored, revised and renegotiated among the economic actors (here owners and executives, or agents and principals).

Coase (1937) and Alchian and Demsetz (1972) formed the point of departure for Williamson (1975) where he developed the contractual relations between corporate actors inside and outside the corporation. In the same way Berle and Means (1932) constructed the platform for Jensen and Meckling (1976) in their work to develop agency theory and addressed in greater depth the relationship between shareholders (principals) and management (agents). This is discussed further in section 3.2.1.

2.3.2 Theory of value creation

In this second part of the concept of the firm the focus is on organizational value creation. The value building processes in most kinds of organizations (including limited companies) can be illustrated using models based on studies of corporate governance and management. This is done in Sjöstrand (1993, 2005 and in Kallifatides, Nachemson-Ekwall & Sjöstrand, 2010) and Östman (1993, 2008) where the idea of a theoretical model that singles out two primary flows of the value building process is developed. This idea is here expressed in *Figure 1*. The authors Sjöstrand and Östman have named the first of these two primary flows as the "operational", and it is usually regarded as a part of an industrial "value chain" and often described in the form of a horizontal arrow. Actors in this operational flow are, for example, employees, various kinds of consultants, local politicians, union representatives and customers. The basic driving forces behind the operational flow include the demand-pull from customers and/or the R&D push from scientists and development managers. Basically, the operational flow represents business enhancement through the locking in of specific resources for a certain period and thereby adding value. Sjöstrand and Östman have named the other core flow, the ”financial” or ”capital” based. They see it as a part of a financial ”allocation chain”, and it is often described with a vertical arrow. The ultimate driving force of this flow is the capital market. This flow is hierarchical in character and cuts across several organizational levels including the shareholders, boards and management.

Figure 1.Two governance flows



Östman, 1993; Sjöstrand, 1993, 2005; Kallifatides et al., 2010

According to Sjöstrand and Östman the two primary flows also compete with each other to gain the upper hand in each organization's governance process. Either capital is allocated for operative value creating activities within the company's boundaries or capital is brought back to the financial flow as dividends or share-buy-backs for new allocation processes (or consumption). Östman (1993, 2008) writes that actors in each flow request different kinds and amounts of financial information (e.g. in the operative flow actors look for possibilities to measure internal efficiency in the processes, while in the financial flow the actors look for figures that make comparisons with alternative usages of capital possible).

Moreover, most actors in the financial flow (particularly those working outside of the focal organization) try to make as much information as possible public (or known exclusively to them) and tend to prefer quantitative data, while those working in the operative flow (particularly the internal actors) try to keep as much of the important information as possible hidden to preserve competitive power. They also possess a great deal of qualitative information.

In the small entrepreneurial company, where one person is both owner and CEO the balancing of the two core flows is simple. This construct has been a platform for theorizing about the firm since the emergence of neoclassic economic research. However, in large companies the situation is much more complicated; the organization is more complex and the entrepreneur replaced by shareholders and managers. With such corporate sizes and a more dispersed ownership, a separation between the controlling and the executive roles occurs. In such cases, an employed *manager (CEO)* has to interpret the will(s) of other actors – the *shareholders*. The role of the other executive body, a *board of directors*, is to integrate the two perspectives – that of the shareholders (a financial rationale) and that of the managers (an operative rationale).

Many internal and external actors influence the allocation of capital (financial resources) to the financial flow (i.e. vertical arrow in Figure 1). The actors that are involved in the allocation of the capital generated from the operational activities (through e.g. profit) have two possibilities. Either they move that capital (in financial form) to more productive investments outside the corporation or they re-invest them within the organization to improve the corporation's operative processes. The ultimate actors in the financial flow, the shareholders, have different agendas, investment horizons, competences and preferences for risk-taking. They might be long-term or short-term in their preference. They might be a private speculator or a sovereign state with a specific ownership objective. It is the board's role to interpret this set of wills into a common goal communicable to the CEO. The ability of specific shareholders to influence the board in this process depends on the institutional environment. Legal systems also differ between countries, while traditions and historical processes influence the power allocated among different groups – the management, board and shareholders voting at the annual general meeting, AGM. There is also a continuous conflict between different shareholders, and the market for corporate control both enables new investors to replace old investors and allows new investors to challenge incumbent management by presenting a hostile bid and enhancing shareholders to sell.

Sjöstrand (1993, 2005; also in Kallifatides et al., 2010) and Östman (1993) point out that it should not be assumed that either of the flows is preferable – the proper functioning of both are necessary for the survival of any organization. The crucial issue is which of the two flows dominate the governance processes in an organization and where – on what hierarchical level – the two flows and perspectives meet and integrate. In the book *Corporate Governance in Financial Capitalism* (Kallifatides et al., 2010), the Sjöstrand-Östman model is approached in some detail. The governance of the corporation is described there as a social process influenced by the three forces – actors, institutions and culture. As this dissertation addresses the cross-border hostile takeover and the processes influencing the board's activity in this setting, the main focus here is on the governance process of the vertical financial flow.

2.3.3 Theory of governance models

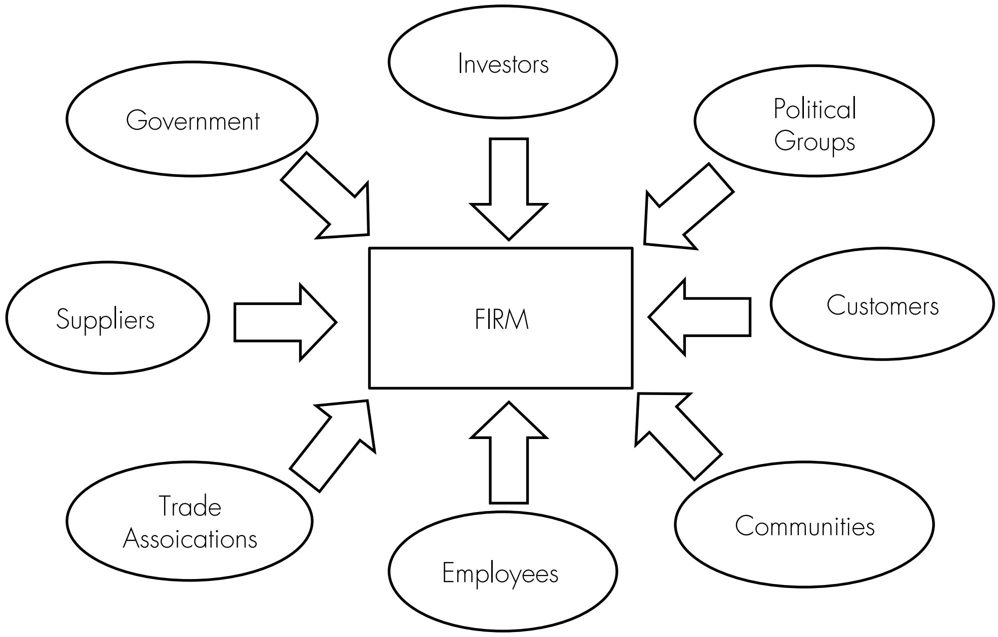
Some kind of a limited liability company, recognition of organizational hierarchies and a separation of control between owners and managers, is to be found in all developed market economies with functioning ideas about institutions. However, the approaches to governance differ. This is the focus in this third part of the firm as a concept behind the hostile takeover. This is reflected in various approaches to the market for corporate control, including the construction of a hostile bid mechanism. As shown in the *Varieties of capitalism literature* (e.g. Coffee, 1991, 2000; Sjöstrand, 1993; Hall & Soskice, 2001) there exists a broad variation of corporate governance models, reflecting different models of capitalism, embedded in different legal systems and in local contexts. There exist two main groups of governance-models, the stakeholder model and the shareholder model. These can be approached as two ideal types.[16]

The *stakeholder model* is present in most countries and often referred to as the inside model. It includes settings based on banking finance, family companies and state involvement. In the stakeholder model of governance, presented in *Figure 2*, the board of directors and the executive management are held accountable to different constituencies. Directors and the executive management regard the interests of both external parties (i.e. the local society, customers) and internal parties (i.e. employees) (Freeman, 1983).

Stakeholder theory is often referred to as an input-output model of the firm, where firms are seen as converting investor, supplier and employee inputs into customer outputs (Donaldson & Preston, 1995). The role of management is to set priorities among different stakeholder interest, to achieve a common whole in the interest of the corporation. Stakeholder theory is normative. It recommends ideals, structures and practices and requires that simultaneous attention should be given to the interests of all stakeholders.

[16] The expression ideal types stems from sociologist Max Weber (1922/1983). It is not meant to refer to a perfect thing, a ”best” thing or moral ideal, but rather to stress certain elements common to most cases of the given phenomena. In using the word “ideal” Max Weber refers to the world of ideas (*Gr:* “Gedankenbilder” or "thoughtful pictures") and not to perfection; these “ideal types” are ideal constructs that help put the chaos of social reality in order; also in Sjöstrand, 1985, p. 14.

Figure 2. Corporation and its stakeholders



Source: Donaldson and Preston, 1995

Modern treatment of stakeholder theory integrates both a resource-based view and a market-based view, and adds a socio-political level.[17] This is reflected in the *OECD Principles of Corporate Governance* (1999), which addresses the interests of all different stakeholder groups. Controlling shareholders – represented by blocks of shares held by families or banks – are viewed as one stakeholder among several. At the same time, shareholders as a group, as residual claimants, remain the most important stakeholder, and are thus empowered with special rights to govern the corporation, through voting at the AGM on certain issues and empowering the board with elected directors. The stakeholder model of governance is reflected in the Continental and Nordic European governance

[17] The origins of the resource-based view can be traced back to Coase (1937), Selznick (1957), Chandler (1962, 1977), and Williamson (1975), where emphasis is put on the importance of resources and their implications for firm performance.

tradition. Within this model control is often allocated to blockholders or actors supported by crossholdings, pyramiding, differentiated voting-power structures and so forth. In this environment the German system which grants the employees the right to nominate directors to half of the seats on the supervisory board, can be seen as an extreme form of stakeholder ship (Roe, 2003; Gourevitch & Shinn, 2006). Other stakeholder models include different forms of state-capitalism, including the French and Japanese models (Roe, 2003). The focus here is on the works of stakeholder systems during the sixth takeover wave, and during this period most of the national stakeholder systems had been reformed through adoption of features from another model, the shareholder model.

The *shareholder model* is often referred to as the ”external model”, relying on liquid capital markets and with its origin in the Anglo-American legal context (Hall & Soskice, 2001). In 1970 influential economist Milton Friedman wrote that: “The social responsibility of business is to increase profits” (Friedman, New York Times Magazine, 13 September 1970; referring to his book *Capitalism and Freedom*), and with this implying that it is the role of governments to set the framework for companies, i.e. laws, to offer education and so forth, whereas the company’s responsibility is to generate money which will then contribute to welfare in the form of profits and tax. The term “shareholder value” can otherwise be traced back to Rappaport (1986), in which the focus is on the cost of capital as a means of distributing financial resources among different targets of investment. The idea is that shareholders’ money should be allocated to the assets with the potential to deliver the best return, given the same amount of risk. For a publicly traded company, with a separation between owners and managers, shareholder value is the part of its capitalization that belongs to the equity side. This means that liquid capital markets, through which listed companies can rely on external financing for raising equity capital, can be viewed as a necessity for making the shareholder-value model of governance to work. Focus on shareholder value implies a governance model that asserts, on the grounds that prices reflect the scarcity of resources; that a management of a corporation aims at maximizing shareholders’ wealth (Tirole, 2006, p. 58).

In the same way as there exist different models for stakeholder governance there also exist different models for shareholder governance. In an environment open for an extreme usage of either model, in the hypothetical sense of an ”ideal” stakeholder model or an ”ideal” shareholder model, new and often unexpected problems emerge. An extreme form of stakeholder governance will complicate the directors' interpretation of their fiduciary obligations, as they feel forced to balance the interests of different stakeholders. The board and management can use that to insulate themselves from the influence of shareholders. In the extreme case the annual general meeting might not be able to hold the board accountable to the shareholders. On the other side, an extreme focus on shareholder governance, i.e. *maximizing shareholder value*, might bring with it governance that only looks after the interest of present shareholders. In the extreme case, liquidation of corporate resources or the sale of part or the whole of the company to the first available buyer will maximize short-term wealth creation.

The focus here then lies on neither of the models. Rather, an institutionalist perspective that integrates theory of social embeddedness and path dependency makes it possible to envisage a national governance regime that constitutes a mixture of governance devices drawn from both shareholder and stakeholder sources. Changes within a system (i.e. through importing shareholder features to previous stakeholder oriented economies) have implication for the value-building process of the corporation (see Ch. 5 for a detailed description of the Swedish, the UK, the US and German models).

2.4 Concept 2: Financial capitalism

Financial capitalism emerges as a second concept making up the theoretical frame of reference of the hostile takeover. A central theme for the establishment of a market for corporate control is the idea that the stock market reflects a correct market value of the listed firm, thus enabling trading in stocks that are correctly priced. Behind this stands the assumption that actors are rational i.e. utility-maximizing investors. As such, prices in the long run will reflect the correct value, or at least the expectations of the correct value. Three theories of finance can be said to have revolutionized the field of economics both in the way external parties derive this value of the firm and how stocks subsequently are traded to maximize return for a given investor. First, there is the early development of the corporate finance field with the Modigliani-Miller theorem (1958) of capital structure as irrelevant to corporate value. From this follows that it is possible for corporate managers to optimize capital costs for any given investments by choosing the right allocation between equity and debt financing. Excess capital can then be returned to investors to be allocated to other, more value accretive investments. Relating back to the Sjöstrand-Östman-model, corporate finance theory equips corporate governors with an instrument to allocate financial resources within the organization in a more optimal way than was possible previously.

The second finance theory is *modern portfolio theory* (MPT), which states that investors can reduce portfolio risk simply by holding combinations of instruments, such as stocks, that are not perfectly positively correlated. Diversification enables the individual investor to choose the level of risk-taking linked to a given index of instruments, i.e. MSCI Large Cap. These ideas began with Markowitz (1959) and were then reinforced by other economists and mathematicians.

The third theory is the *efficient market hypothesis* (EMH) developed by Fama (1970). It builds on the idea that all available information is incorporated in the market price of a tradable unit. The EMH rests on three assumptions:

- Investors are assumed to be rational and as a result to value securities rationally.
- To the extent that investors are not rational, their trades are random and will cancel out each other without affecting prices.
- To the extent that the investors are irrational in similar ways, they are met in the market by rational arbitrageurs who eliminate their influences on prices.

Market participants have well defined subjective utility functions that they will maximize. The EMH asserts that financial markets are ”informational efficient”. One cannot on a risk-adjusted basis consistently achieve returns in excess of average market returns. Fama (1970) claims that there exist levels of efficiency – strong, semi-strong and weak and the equity market is generally assumed to be efficient in the two latter forms.

Since its emergence, the EMH has been the most important theory for explaining the behaviour of the various agents in the financial markets though it neglects of almost any potential impact of human behaviour in the investment process. This financial theory influenced the neoliberal economic and globalization movement that started in the 1970s and continued to dominate well up to the financial crisis of 2008. The movement included a reshaping of previously captive markets, an abandonment of credit market and currency regulation and an opening up for the development of a globally active investment industry for institutional investors. Such “well functioning” financial markets were also seen as a prerequisite for the emergence of an efficient market for corporate control, that enables hostile takeovers (see next section 2.5).

The influence of financial theory on the world economy has become so profound that it can be viewed as having constructed a whole new era of the world economy, *the age of financial capitalism*. From a corporate perspective this financilization of the corporation can be contrasted with the previous era of managerial capitalism in the US and in the UK, and industrial capitalism in Continental and northern European countries, including Sweden.

However, that has not passed without criticism. From the end of 1970s and the beginning of 1980s, a growing number of theorists showed the existence of serious anomalies and drawbacks of this theory. Among other things, this resulted in the emergence of a new strand of research *behavioural finance* that integrates psychology and economics into finance theory (i.e. Kahneman & Tversky, 1979). Behavioural finance includes research on emotions, herding, groupthink, heuristics and so forth. It draws extensively on Simon’s notion of bounded rationality, where decision-making in an organization was explained. It can also be applied to investor’s decision-making on capital markets. Shleifer (2000) points out that investors' attitudes toward risk, their non-Bayesian expectation formation, and their framing of problems, make them deviate substantially from classic economic models of rationality. Other researchers linked the financial theory of the late 20th century to the recurrent bubbles and crashes of western capitalism (for a description of equity-bubbles see e.g. Parenteue, in Epstein, 2005). Despite this critique, the EMH has remained a main theme in financial capitalism.

Seen from an institutional perspective, the meaning of financial capitalism goes beyond the importance of financial intermediation (as seen in the quest of liquid capital markets) in the modern capitalist economy. As part of a social process it also encompasses the significant influence of wealth holders on the political process and the aims of economic policy. Epstein (2001, p.3) defines *financialization* as: "…The increasing importance of financial markets, financial motives, financial institutions, and financial elites in the operation of the economy and its governing institutions, both at the national and international levels."

The idea of the EMH and the subsequent financialization of the western economy have largely been blamed for having started the financial crisis in 2007 (for early accounts see Cooper, 2008; Schiller, 2008). This is beyond the scope of this dissertation, which limits the analysis to the implication of the EMH in relation to the value building process of a firm targeted during a cross-border hostile takeover process.

2.5 Concept 3: Efficient market for corporate control

The third concept of the complex institutional organizing of cross-border hostile takeovers is the idea of a market for corporate control. A hostile takeover can be described as the pursuit of a bid by a bidder, i.e. suitor, to take over a target company without the consent of the target's management or its board.[18] A takeover is considered hostile if the target company's board rejects the offer, but the bidder gets target shareholders to accept it in any case. Takeovers that are not classified as hostile are denoted *friendly* takeovers.

The market for corporate control could be described using mainstream finance with its notion that to be efficient it has to facilitate mergers and acquisitions and that this *per se* creates welfare for society at large. A free market for corporate control, with its openness for both friendly and hostile takeovers, disciplines managers of corporations to act in the best interest of the shareholders (Macey, 2009). Badly performing management will see its share price fall, thus, threatening managers with the risk of a takeover on such a market; where "better" companies and managers take over "bad" companies and managers. This approach builds on Henry Manne's seminal article from 1965, *Mergers and the market for corporate control*, with its view of hostile bids as an effective means for ”disciplining non-value-maximizing managers”.

> ”As an existing company is poorly managed… the market price of the shares declines relative to the shares of other companies in the same industry or relative to the market as a whole…The lower the stock price, relative to what it could be with more efficient management, the more attractive the takeover becomes to those who believe that they can manage the company more efficiently, and the potential return from the successful takeover and revitalization of a poorly run company can be enormous…" (Manne, 1965, pp. 112-113)

In line with this reasoning, supporters of hostile activity argue that a hostile bid is often the only effective mechanism for removing corporate control from entrenched, inefficient management. With this in mind, actual

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[18] The takeover literature uses a number of different words to describe the actors involved, where ”suitor" is one. The legal terms for ”bidder", ”bid" and ”target" are ”offeror", ”offer" and ”offeree". ”Bidder" is used in most common texts, such as media reporting, whereas ”offeror" relates to legal texts such as takeover regulations and public statements from a party presenting an offer/bid. Here I will mostly use ”bidder" and ”target".

hostile activity may not even be necessary to produce positive effects: If the probability of a bid increases with managerial misconduct, and if deviating managers are punished sufficiently in the event of a change in control, then the mere threat of a hostile bid makes managers less prone to slack. Thus, on an active takeover market that enables hostile takeovers, shareholders are given an instrument (current stock price) through which they better can monitor the work of the CEO, a "torture instrument" so to speak (Windolf, 2008, p. 20). Conversely, protective measures that hinder shareholder influence and complicate hostile bids, such as staggered boards, limits to shareholder bylaw amendments, poison pills, golden parachutes, and supermajority requirements for mergers and charter amendments, all contribute to lowering stock market price, and thus work to destroy shareholder value and hamper efficient capital allocation among corporate constituencies (Bebchuk, 2002; Bebchuk, Cohen & Ferrell, 2004).

However, to fully grasp the hostile mechanism a more detailed theoretical discussion is necessary. Manne (1965) goes back to Smith (1776), the so called *invisible hand* with the creation of perfect capital markets, and the natural quest by companies to grow and merge into entities large enough to create a monopoly power. To prevent this socially undesirable behaviour (as the price-supply-mechanism is distorted), the US during the middle of the 20th century developed regulatory antitrust limits to mergers. Cartels were forbidden. Horizontal mergers in particular were addressed as these automatically reduce competition. However, Dewey (1961) notes that most takeovers in the US at the time had very little to do with either the creation of market power or the realization of scale economies. Dewey claims that: "If the capital market was perfect and a merger confirmed no monopoly power, a rising firm would be indifferent between the two forms of expansions" (Dewey, 1961, p. 257). Rather, most mergers seemed to be "A civilized alternative to bankruptcy or the voluntary liquidation that transfer assets away from failing to rising firms…" (Dewey, 1961, p. 261)

The first attempt to formulate a theory of takeovers was made by Marris (1963) with the proposal that takeovers promote economic natural selection and that its threat constrains managerial behaviour. In contrast to his contemporaries, Marris claims that the selection process results in the survival not of profit maximizing firms but of those that maximize growth.

Building on both Dewey (1961) and Marris (1963), Manne (1965) argues that M&A activity can be desirable even if there is no risk for bankruptcy. Instead the control of corporations may constitute a valuable asset, because this asset exists independent of any interest in either economics of scale or monopoly profits, because an active market for corporate control exists and because many mergers are probably the result of the successful workings of this speciality. Manne (1965) lists five benefits of a well functioning market for corporate control:

1. Lessening of wasteful bankruptcy proceedings.
2. More efficient management of corporations.
3. Protection to non-controlling corporate investors.
4. Increased mobility of capital.
5. Generally a more efficient allocation of capital.

Just like Berle and Means (1932) dispersed shareholdership and managerial corporation, Manne's market for corporate control is intertwined with the notion of liquid capital markets. However, there are also certain differences. Manne list three fundamental preconditions underlying the market for corporate control:

- There exist a high positive correlation between corporate managerial efficiency and the market price of shares of that company. This will hold true over a period of time, as the market price will more or less reflect true value, and there are no other real measure of managerial efficiency.

- A dispersed set of shareholders, viewed as pure (profit-maximizing) rational-financial investor in a Berle and Means sense, that have the right to sell to another buyer when dissatisfied rather than relying on either the the fiduciary duties of directors and management or the business judgement rule (see section 5.5 and 6.6).

- Berle's contention that control is a corporate asset is wrong. The implication of Berle's notion is that any premium received by an individual for a sale of control belongs in equity to all of the shareholders.

The three preconditions stated by Manne have had important implications for the development of hostile takeover theory and regulations going forward. The first precondition targets the very fundament of liquid capital markets and the Fama (1970) efficient market hypothesis. Assuring that all actors have access to relevant information at the same time becomes an important factor to be overseen by policy makers and regulatory bodies. "Transparency", as to both minimize insider trading and assure equal treatment of different shareholder groups thus emerge as a prerequisite for a well functioning market for corporate control.

The second precondition of dispersed ownership in Berle and Means fashion is refined by Hirschman (1970) in the book *Exit, Voice and Loyalty* claiming that a prerequisite for the development of an efficient market for corporate control is that the shareholder in a publicly listed company can make three choices – continue as owner and try to exert influence over the board's decision by voting at the general meeting, do nothing and remain a passive owner of shares without exercising the right to vote or sell the shares to someone else.

The third precondition differs from the two others in the sense that the first two preconditions address the market and actors, whereas the third precondition deals with the fundamental idea of the corporation. Thus, Manne (1965) brings corporate law into the model. The Berle and Means (1932) argument that control is a "corporate asset" implies that premiums paid for control go into the corporate treasury. The issue of "corporate asset" is discussed by Berle and Means (1932) in connection to a critical comment on a ruling by the New York court in relation to damage done to minority shareholders during a change of control. In

Berle and Means, 1968, p. 216-217:

> "But it apparently involved too great a leap in the dark for the New York court to say that the power going "with" control is an asset which belongs only to the corporation; and that payment for that power, if it goes anywhere, must go into the corporate treasure…the law thus far has been unable to deal with the situation."

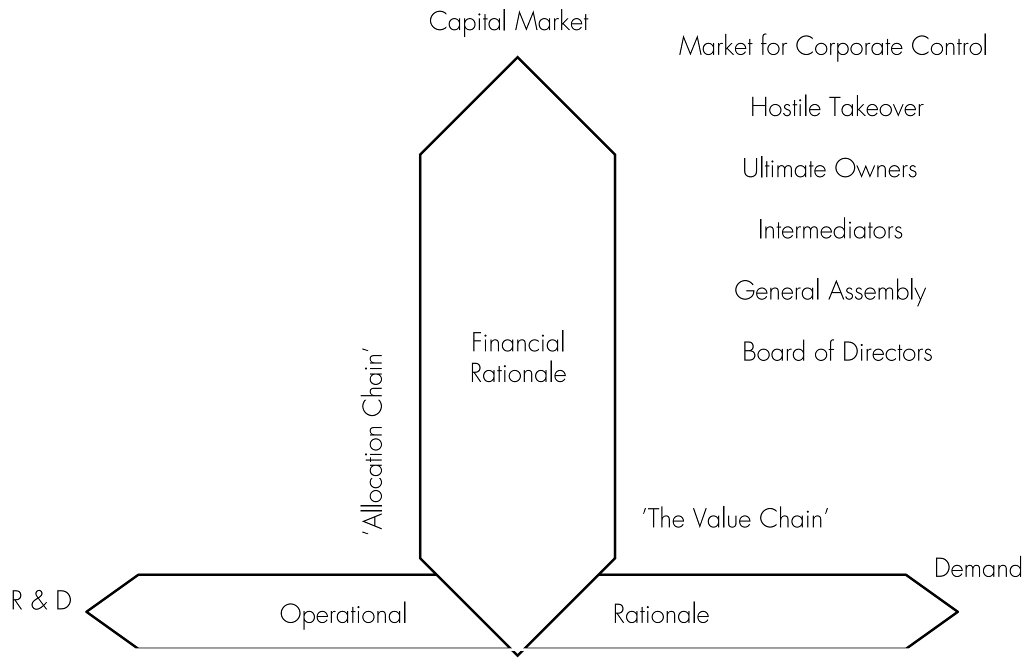
Early supporters of this Berle and Means idea equate *fair* treatment with *equal* treatment of shareholders. This *equal opportunity* rules that minority shareholders should be entitled to sell their shares on the same terms as the controlling shareholder (Jennings, 1956; Andrews, 1965). Manne (1965), however, objects to this, claiming that actors that own control blocks of shares might refuse to sell at a share price which does not pay them a premium at least sufficient to compensate them for the loss of net value presently in participating in the governance of the corporation. If all shareholders will get the same price, Manne claims, control contests will be more expensive and there will be fewer changes of control (i.e. less value accretive restructuring beneficial for society). In this dissertation *the Manne vs. Berle and Means* debate will remain a central theme in the development of an understanding of a market for corporate control.

Viewed together, the three preconditions of a Manne-efficient market for corporate control stipulate that the shareholders active on a liquid capital market are in full control of the financial flow of the corporation. Thus, it goes without saying that stakeholder governance in the interest of a multiple of constituencies has trouble dealing with financial theory and its ideas of an efficient market for corporate control that facilitate hostile takeovers in the interest of only one stakeholder group – the current shareholders.

Manne (1965) also elaborated on the choice between different methods employed on the market for corporate control contests – proxy fights, direct purchase of shares or mergers. Manne settled for mergers as the most efficient as it both protected value for non-controlling shareholders and assured takeovers from a general value accretive economic point of view. This is worth bearing in mind, as the Manne's hostile bid never was meant to be anything but an uncommon event on the M&A market.

As a pedagogical exercise I summarize this theoretical discussion with an application of the Sjöstrand-Östman model (Ch. 2.3.2) to the hostile takeover market in financial capitalism and thus include this agency in the governance process. In *Figure 3* the financial rationale is expressed as a two-way flow, indicating the inclusion of external forces into the model or, put differently, the destabilization of the model.

Figure 3. Two corporate governance flows applied to a hostile takeover



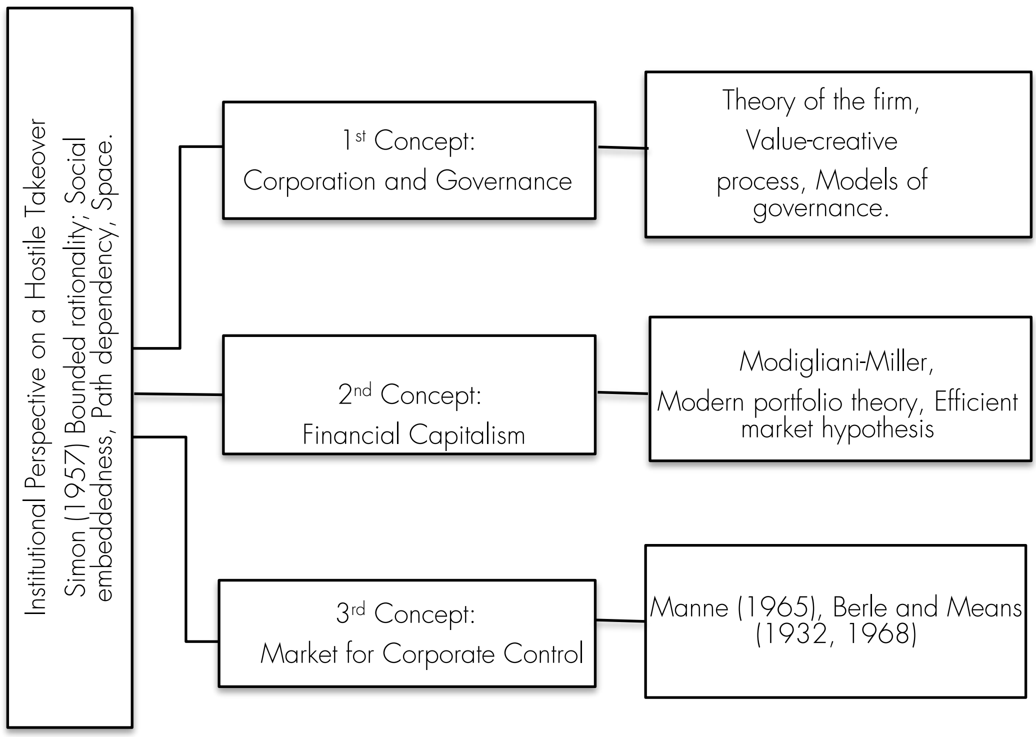
This application of the Sjöstrand-Östman model includes the board of directors in order to highlight different forces influencing their activities during a hostile takeover process. The target company board is influenced by the idea of the perfect market and the idea of the rational and utility-maximizing man. As can be expected the model quickly becomes very complex. Among institutions influencing the market are capital market regulations, both domestic and supranational, as well as various self-regulatory bodies. As for the individual director, his or hers behaviour is influenced by corporate law, models of corporate governance, norms as well as codes. It is not always the case that these institutional frameworks are compatible, and this will form the starting point for the second part of the theoretical chapter, Ch. 3.

2.6 Conclusion

This chapter has used an institutional perspective to present a theoretical frame of reference to the hostile takeover process. This frame (below in Figure 4) is based on three concepts – the corporation and governance, financial capitalism and the market for corporate control.

An institutional perspective of the market for corporate control brings together theories from law, management, economics and finance. In doing so, the idea of the utility-maximizing and rational actor is replaced by a more complexly constructed human being. This human is also equipped with feelings and bounded rationally gathering information to the extent that it delivers a satisficing result. This view has deeply influenced the formation of organizational research and the development of management literature. Turning to the limited company, it is an organizational unit with boundaries that enables a value-building process to emerge. It has proven to be a fantastic economic machine capable of wealth creation to the benefit of society at large. The governance of this machine is a complex matter. In the simple firm, run and owned by an entrepreneur, it is fairly straightforward. However, complications emerge when the firm grows, a CEO is recruited externally and there are multiple and often distant owners. The firm can then be described as a complicated hierarchical structure difficult to govern by distant owners.

Figure 3. Theoretical frame of reference of a hostile takeover



In the value accretive entity of a firm there is a continuous fight between the different rationalities governing the operational flow (where the company meets suppliers, employees and customers) and the financial flow (where the company meets actors on the capital market). These different rationalities are dealt with through corporate governance. Embedded in different domestic systems two broad groups of governance models can be said to exist, the stakeholder and the shareholder models. In reality most domestic models are composed of ingredients from both ideal types. Contractual scholars claim that it possible to govern this entity by simultaneously co-ordinating the separated decision-making through contractual agreements between parties. This makes decision-making a matter of a principal-agent relationship, where the shareholder acts as principal and management takes the role as agent.

In the 1960s mainstream finance with theories built on risk arbitrage, portfolio-asset models and the efficient market hypothesis (EMH) revolutionized modern economic thinking. This greatly influenced the neoliberal free-market economic and globalization movement that started in the 1970s. Theories of the creation of a market for hostile takeovers developed parallel to this thinking. Manne's idea from the 1960s of the hostile takeover as an effective means for "disciplining" "bad" performing management teams, to be contested by "better" performing management teams has since laid the ground for the hostile takeover as a value accretive device.

The creation of an efficient market for corporate control, which enables (cross-border) hostile takeovers, presupposes that the EMH works. As shown in this first theoretical chapter this is far from a simple matter. Also, Manne's market for corporate control does not address unequal treatment of different shareholder groups, instead being satisfied with a bid premium being paid as to reflect the value of the company whereas Berle and Means (1932) claim that the focus should also be on the premium being equally distributed among all target shareholders. Here, this debate will remain a central theme in the theoretical development of an understanding of a market for corporate control.

Many of the assumptions behind the EMH, such as the existence of an utlity maximizing rational human being and capital markets reflecting correct prices, have pushed critical financial scholars in the direction of psychology and behavioural finance. Others have turned to institutionalism, looking for societal factors such as national embeddedness and path dependency as governing the forces behind the hostile takeover-process. It is that more complex view of how the market for corporate control works which is applied in the following. Exactly what these forces might be, how they have influenced democratic decision-making bodies and what regulators have done is the subject of the second theoretical chapter.

Chapter 3

Theoretical drivers for policy makers

3.1 Purpose and structure of this chapter

This chapter makes up the second part of the theoretical introduction. It builds on the theoretical framework developed in Ch. 2 and outlines the theoretical drivers for European policy makers in their work with *levelling the playing field* among corporate actors across Europe with the over-arching aim of creating an efficient market for corporate control that enables cross-border hostile takeovers. I highlight three theoretical drivers that I claim to be present in cross-border hostile takeover processes. The first driver is the quest for the development of a coherent system for corporate governance. This has led European policymakers to push both "soft" and "hard law" in a direction away from stakeholder governance to a shareholder model of governance. Playing an important role in this shareholder orientation is the integration of financial economics and the adoption of the concept of agency theory including contractual theory.

The second driver relates to building a common regulatory framework that supports a cross-border market for corporate control. This has focused on two potential agency problems during a takeover-process. The first agency problem addresses the role of management vis-à-vis shareholders of the target company (i.e. the principal-agent conflict).

This problem relates to firms with dispersed shareholders such as the Berle and Means firm. The other agency problem concerns the role of the bidding party vis-à-vis target investors and the relationship between different groups of target investors. This problem relates to firms with a controlling block holder (i.e. the principal-principal conflict).

The third driver stems from the institutional investor such as pension and retail funds, a group that has emerged as dominant actors on capital markets in modern financial capitalism. Regulated and incentivised to follow different indexes they have developed a rather haphazard investment style focused on short-term investment strategies.

Each section below includes an analysis of the implications each driver has had for the outcome of a cross-border hostile takeover contest, for the creation of a level playing field on the one hand, and for the value accretive process of the firm on the other hand. These implications are formulated as seven propositions. In a final attempt to build a theoretical model that enables an understanding of the three drivers for policy makers of a cross-border hostile takeover process, the chapter concludes with a presentation of a framework built on institutionalism. This is done with reference to Aguilera et al. (2003) and Aguilera and Jackson (2007). In the concluding section 3.6 the seven propositions are transformed into three hypotheses. These hypotheses summarize the three drivers of the cross-border hostile takeover process addressed in this chapter as:

- The political-regulatory elite is conducting a one sided quest for a shareholder value model of governance.
- There exists regulatory and moral arbitrage between actors from different governance systems.
- Short-termism appears to drive investment strategies of institutional investors.

3.2 Driver 1: Corporate governance

3.2.1 Shareholder model and agency theory

The first theoretical driver for policy makers in the quest to create a pan-European market for corporate control addresses shareholder value and the preference of this governance model. As stated previously the shareholder model is referred to as the external governance model, relying on liquid capital markets. It has its origin in the Anglo-American legal context (Hall & Soskice, 2001) with its prevalence of Berle and Means type firms, i.e. firms with dispersed shareholders and control in the power of management. It is best understood in relation to agency theory, a framework for governance that integrates elements from the theory of agency, the theory of property rights and the theory of finance to develop a theory of the ownership structure of the firm. Presented in a number of articles by Michael Jensen during the 1970s and 1980s (e.g. Jensen & Meckling, 1976; Fama & Jensen, 1983) agency theory dominated the governance discourse in the USA from the 1980s and in Europe from the early 1990s at least until the financial crisis of 2008.[19]

Jensen and Meckling (1976) studied conflicting objectives between investors as shareholder-owners of the company's equity and participants such as the firm's management. Their intention was to learn how these conflicts could be brought into equilibrium so as to yield the maximum result for investors in the form of maximum return on equity, profit in the form of dividend or present value in the form of market value. To refine the behavioural implications of the contracts between owners and managers of the firm, Jensen and Meckling addressed the problems of monitoring team production that Alchian and Demsetz's raised in their paper on *The theory of the firm* (1972).

[19] In a review of more than 1 000 publications on corporate governance research from the period 1993-2007, Dursin and Puzone (2009) find that agency theory dominates the research on corporate governance.

Jensen and Meckling defined an agency relationship as a contract under which one or more persons (principals) engage another person (agent) to perform some service in their interest. This involves delegating some decision-making authority to the agent. If each party tries to maximize their subject utility, there are good reasons to assume that the agent will not always act in the best interest of the principal. This might lead to inefficient usage of corporate resources. Examples of this behaviour are inefficient investment decisions, through for example empire building, entrenchment, with resistance to takeovers as an example, and insufficient effort into the form of shirking or various kinds of self-dealing including perks, sweetheart deals and looting.

The information problem between the principal and the agent is described in terms of a problem of asymmetric information, adverse selection and moral hazard. The question becomes how to detect and limit agency costs and how to structure them. Jensen and Meckling define agency costs as the sum of monitoring expenditure by the principal, bonding costs by the agent and residual cost. Among costs are enrolment of independent directors and public accounts. However, some inefficiency will remain.

Fama (1980) relies heavily on Jensen and Meckling (1976) to discuss how the agent uses asymmetric information to take on risks for which the principal carries the greater cost. For Fama (1980) managerial opportunism emerging from the information gap is curbed through an efficient labour market for managers. Fama (1980) and Jensen and Ruback (1983) saw the need to discipline firms through both competition from other firms and the establishment of independent boards with efficient monitoring of the managers, but they develop this further by turning to executive pay, in stocks and options, as the prime disciplinary factor to align management interest with those of shareholders. This reasoning is developed through econometrics and delivers a financial model of the right way to incentivize managers.

Leaning on the shareholder model the Jensen and Meckling agency theory and the minimization of agency costs emerge as a disciplining approach to assure financiers that they receive the correct and expected return on their financial investment (Shleifer & Vishny, 1997, p. 703).

Summing up, these drivers for external shareholder governance, available to minimize agency costs (to be able to maximize shareholder value) can be claimed to belong to three groups:

- Executive compensation programmes.
- Board composition to enable efficient monitoring in the interest of the shareholders.[20]
- Competitive product markets.

Hostile takeovers are seen to be a fourth governance mechanism, where shareholders play the role of a passive audience (only legally involved), as the value accretive work of incumbent management is contested by other management teams (Jensen & Ruback, 1983). Thus, the market for corporate control, and the hostile takeover, can be seen as an integral part of the toolbox of shareholder-value drivers for a Berle and Means' corporation.

Viewing the market for corporate control as the arena in which different management teams compete means that the focus in Jensen and Ruback (1983) shifts from the traditional view, in which financiers and activist stockholders are the parties who (alone or in coalition) buy control of a company and hire and fire management to achieve better resource utilization, to a focus instead on the role of management. This *managerial competition model* centres on competing management teams as the primary activists. Arbitrageurs and takeover specialists play the role of facilitators and intermediaries. Stockholders have no loyalty to incumbent managers; they behave passive and simply sell for the highest dollar price. According to Jensen and Ruback (1983) the listed company is unique as a value creator for society as the hostile takeover serves to limit the managerial departure from maximization of stockholder wealth, i.e. focus on shareholder value (alternative institutional forms lack this feature, for example professional partnerships and mutual societies).

[20] Board governance mechanism are often approached in terms of board independence, CEO-chairman duality and board member compensation.

3.2.2 In search of a best governance model

Answering calls from globalized financial markets, modern corporate governance research has leaned towards the shareholder model of governance as the preferred governance model. Institutional investors in particular, such as pension and hedge funds have been vocal promoters of the shareholder-value regime as opposed to stakeholder governance. It is easy to find plenty of examples of that on the US market (Kahn & Winton, 1998; Monks & Minnow, 2008; Gourevitch & Shinn, 2006), on the UK market (Charkham & Simpson, 2003; Becht, Franks, Mayer & Rossi, 2009) and on the Swedish market (Jonnergård & Larsson, 2008). It is also easy to understand why shareholder value appeals to institutional investors, as the principal-agent contractual relationship embedded in the shareholder-value model enables governance to be evaluated and mediated at a distance.

The hostile takeover, or threat of such, plays an important role in the governance process. Jensen (1988) writes that the market for corporate control creates large benefits for shareholders and for the economy as a whole by loosening up control over vast amounts of resources and enabling them to move more quickly to their highest-value use. This was assumed to help the American economy to adjust to major changes in competition (at the time pinpointed as Japanese) and regulation (e.g. telecom and utilities) of the 1980s. Bhide (1989) notes that the vibrant market for corporate control and hostile deals of the 1980s, for many associated with the corporate raiders on Wall Street, were associated with beneficial restructuring. This was successfully continued in the 1990s as corporate actors had learnt the lessons of the 1980s (Holmstrom & Kaplan, 2001). Rajan and Zingales (1998) conclude that countries with better-developed financial systems show superior growth in capital-intensive sectors that rely heavily on external financing.

All this led to the development of a research-strand focusing on the existence of a "best model of governance" where there could be both a choice between the stakeholder-value model of governance and the shareholder-value model of governance and a choice between a Berle and Means dispersed shareholder-structure (i.e. a prerequisite for the hostile takeover to succeed) and an interlocked ownership (i.e. not contestable stakeholder control through cross-holdings or voting differences). The starting point for this convergence literature is usually dated to the articles, Shleifer and Vishny (1997) and La Porta, Lopez de Silanes, Shleifer and Vishny (1998, 1999), commonly referred as the *LLSV literature* with its then highly sensational proclamation that different legal regimes appeared to be able to explain differences in national GDP growth. This is often reflected as a measure of the level of protection offering minority shareholders.

The LLSV articles divide countries into two groups according to the origin of their legal system: common-law countries and civil-law countries. Anglo-Saxon *common law* is based on case law. It is essentially the judges who make the law by creating precedents in court. Conversely, (Continental) European *civil law* is based on codified rules and the judges' function is limited to interpreting the law texts in court. Basing themselves on a range of legal devices, the LLSV authors construct an index of shareholder protection. They conclude that the common law system, which is usually built on a market-based financial system where firms raise funds on capital markets (such as bonds and equity right issues), offer better minority shareholder protection than the civil law system, which is more dependent upon bank-based systems where banks provide most of the credit to the economy, and which has built governance-regimes based on controlling shareholders rather than minority shareholders.

The LLSV articles claim that common-law countries such as the UK and the US, with their liquid markets, shareholder-value orientation and openness to takeovers (friendly as well as hostile), offer a better system of corporate governance than civil law countries such as those in Continental Europe and the Nordic countries. The LLSV articles have inspired a strand of literature arguing that the shareholder-based system is superior as it provides better protection of minority shareholders.

Many studies in financial economics appear to support the theory that liquid markets and a focus on shareholder value (which like the US and British markets attract globally active institutional investors) is associated with lower transaction costs, higher expected returns and a lower cost of capital (Becht, 2003). Liquid stock markets also have the ability to carry capital over "long distances", both geographically and between sectors (Holmstrom & Kaplan, 2001). Based on a survey of 200 listed Swedish companies in 1985-2000, Holmén and Nivorozhkin (2007) found that firms with differential voting rights receive a lower valuation as measured by *Tobin's q*.[21] Bjuggren et al. (2007) found similar results, and so did Barontino and Caprio (2005) for some other European stock markets. Barontino and Caprio also showed that this value discount only holds for separation of control through voting-differentials and not for companies where the controlling owner emerges as a de facto controller of both capital and votes. From a market valuation-perspective there seems to be plenty of support for the institutional investors' push for the abandonment of multiple voting shares (which is a common feature in Swedish governance).

Thus globalization appears to have brought with it a quest for convergence towards the Anglo-American shareholder-value model of corporate governance, as "the best model". The expected result would then be a global convergence in actual corporate governance to the shareholder-value model as the preferred choice (Coffee, 1991; Rajan & Zingales; Bolton & von Thadden, 1998; Berglöf & Burkart, 2003; Hansmann & Kraakman, 2004; Becht, 2003; Burkart & Panunzi, 2008). In that process, the Continental European corporate control model, often based on block holdings, crossholdings, pyramiding and so forth, will lose in attractiveness and companies will move to an open ownership structure with multiple shareholders. According to Hansmann and Kraakman (2004), among the most quoted scholars on the convergence theory, this move reflects the existence of a best solution for value accretive growth worldwide, as the "ultimate control over the corporation should be in the hands of the shareholder class" (Hansmann & Kraak-

[21] *Tobin's q* was developed by James Tobin (Tobin, 1969) as the ratio between the market value and replacement value of the same physical asset. It has become common practice in the finance literature to calculate the ratio by comparing the market value of a company's stock with its equity book value.

man, 2004, p. 35). Other stakeholders (creditors, employees, suppliers and customers) "should have their interest's protected by regulatory and contractual means and not through participation in corporate governance" (Hansmann & Kraakman, p.35).

3.2.3 Critique of the best-model approach

From the perspective of the establishment of an efficient market for corporate control in Europe, the research focus of a "best model" has not been without complication. Academics from within the same research tradition as well as those from differing academic disciplines have continuously debated, not the merits for a common market as such, but the difficulties in establishing a "level playing field" among corporate actors. Here the perceived theoretical shortcomings of the level playing field are dealt with in terms of two contrasts:

- The Manne interpretation of a Berle and Means dispersed shareholder structure, *as compared* to a model with controlling shareholders.
- The focus on agency theory and shareholder-value governance *as opposed* to an approach building on corporate values and stakeholder governance.

Below follows a theoretical discussion of the two complications based on literature from different fields. I begin with delivering seven propositions that then are summarized as three hypotheses, which I then develop empirically. Building on the results I conclude (Ch. 9) with opening up for further testing and development of theory going forward.

The academic discussion of the strength of the shareholder value model of governance is complicated by the existence of different structures of ownership. For example, agency theory might be used as a model for governance for the Berle and Means' company with a dispersed shareholder-structure (as in the US), but it does not offer an explanation for the value accretive process that occurs in a company with more concentrated ownership structure. Dealing with this issue, Aghion and Tirole (1997) extend on agency theory by developing the theories of allocation of formal authority (the right to decide) and actual authority (the effective control over decisions) within organizations. Using Weber (1922/1983) and Simon (1957), Aghion and Tirole (1997) claim that the allocation between formal and actual authority rests upon asymmetric information and bounded rationality, as delegation is always the case when there is separation between managers and workers. According to Simon (1957) decision-making requires information, and this is why formal authority differs from real authority. The important question is then how to design it (reduce internal agency costs) and how to allow for flexibility and change. Thus, some degree of independence, Aghion and Tirole argue, might be necessary for management, otherwise it might not wish to perform. With this perspective, a blockholder could mitigate the agency-conflict as some of the information instead is delegated to the owners.

A situation in which there are minority shareholders and shareholders that act as block holders is highlighted by Grossman and Hart (1980), who address the relationships among actors on the market for corporate control, shareholders' role as free riders and the incomplete contract discussion. Here the question is how the shareholder model addresses the situation with blockholders rather than a more dispersed shareholder structure, built on the idea that the assets of the company during a takeover situation belongs to all shareholders alike (i.e. the Manne *vs.* Berle and Means discussion). On the positive side, Grossman and Hart (1980) claim that minority shareholders can free ride on a controlling shareholder's work with enrolling board members and exercising influence at the board. However, on the negative side, a block holder often has ample opportunities to exert influence over the allocation of corporate resources in the interest of the block holder, thus receiving advantages at the cost of minority shareholders. In addition, using property rights and contractual arguments in line with Alchian and Demsetz (1972), the block holder can use its right as owner to sell its part of the cash claim of the firm at a premium to an outside party, leaving the minority either on its own with a new controlling shareholder or having to accept a less appealing price.

The cost associated with the freezing-out of minority shareholders is often described as tunnelling or rent seeking.[22] It can also be seen as a simple transfer of corporate value to one party. Gilson and Black (1995) describe the minority shareholders' available options as a governance situation were it is rational to support the blockholder as long as the minority shareholder believes the value of a controlling shareholder is higher than the costs for private benefits of control.

The "best-model" approach to corporate governance can also be criticised from an institutional perspective. Legal scholar Coffee (1999) argues that dispersed shareholdings in the US primarily were the results of US legal development around the turn of the century, which limited activities of banks and instead promoted market activities for raising capital. However, this had nothing to do with ideas of value creation in corporations, but was rather a response to a number of scandals, i.e. a result of path dependency and social embeddedness. Over time the misalignment between shareholders and management made US companies less successful than their counterparts in Germany and Japan, where managers could concentrate more on the long-term perspective. As explained further in Coffee (2009), the US regulatory framework should be understood as the result of political constraints, liquidity preference and minority exploitation rather than a superior value accretive mechanism.

Management scholars have from their perspective struggled to come to terms with the last 25 years' academic focus on agency costs as the (only) legitimate way to evaluate board effectiveness. Elaborating on a survey of studies of board behaviour and value creation Huse et al. (2009) propose studies of team production that are designed without the assumption of complete contracts between the directors and the shareholders. If the board's relationship to the shareholders instead is treated

[22] Tunnelling refers to the practise by inside management to order the company to transfer or sell off- corporate assets to a second company, usually run by a related party (a managers or an owner), at an unreasonably low price. Tunnelling differs from outright theft because people who engage in tunnelling generally comply with all of the relevant legal procedures. The term rent seeking developed from the landowner's historical right to extract rent without adding any value (Kreuger, 1974).

like its relationship to other stakeholders, it will be easier to understand, and study, the real drivers behind board actions, which might include such things as identification, social identity, routines and groupthink. Accordingly, actual board behaviour, and the board's ability to contribute to the value accretive process, can neither be understood – nor studied – in relations to a straight contractual relationship as designed through agency theory (Huse et al., 2009).

Other academics in finance question the shareholder-model-governance focus on minimizing agency cost altogether. In Burkart, Gromb and Panunzi (1997) it is argued that since being listed implies a separation of ownership and control some slack is inevitable. Put differently, if the exercise of control is the same when in full control and when there is a separation of ownership and control then the whole idea with listed company does not work! In the Miller-Modigliani world of efficient capital markets the investors are one homogeneous neutral rational group of actors. In reality that is not the case. So there are two parallel agency-conflicts that have to be addressed – between outsiders and insiders, and between different groups of outsiders. Continuing the reasoning of Burkart et al. (1997), a large shareholder constitutes a special case in corporate governance. Monitoring by a controlling blockholder, especially when the voting power is strengthened as a consequence of shares that have been legally granted different voting-power, can be regarded as an efficient instrument to mitigate managerial opportunism, and it can solve the agency-conflict embedded in the dispersed ownership-structure. Summing up, this leaves us with the following two propositions:

> *Proposition 1*: When the company has a controlling shareholder the principal-agent conflict is replaced by a principal-principal conflict. Information asymmetry emerges as a problem of benefits of control, and rent seeking can be mitigated through legal devices protecting minority shareholders both continuously and during a change of control.

> *Proposition 2*: Agency costs are a necessity for the development of the value accretive process in a public company where there is a separation of ownership and control. The question of creating shareholder value becomes more a question of how to design a governance system that can enhance trust in

> such a way as to entice minority shareholders to invest in the company, rather than a question of developing devices to mitigate the conflict.

With this in mind the next section addresses how takeover regulation has developed to deal with these twin agency conflicts, between the principal and the agent and between the principal and principal, with a special focus on Europe.

3.3 Driver 2: Takeover regulation

The second theoretical driver for policymakers addresses the development of takeover regulation and the resulting arbitrage between different systems of governance and corporate law. Manne (1965) argues that the market for corporate control and its openness for friendly as well as hostile takeovers promote efficient utilization of corporate resources. But Manne describes a takeover market in its very infancy, far from the present day mechanisms in place to enable hostile takeovers. Manne's takeover market lacks institutions, such as strong (legal) protection for investors, transparency, disclosure and unbiased enforcement of contracts. Nor does Manne address situations when management tries to fight off a bid but shareholders sell, or situations that emerge when a bidding party makes a partial bid, leaving some incumbent shareholders without an offer, or when a large blockholder sells its shares without support of either management or other shareholders. This means that Manne's efficient market for corporate control does not emerge as a spontaneous order. It is a *product of law*. Thus, takeover regulations that enable hostile bids in the interest of society must take a number of different dimensions into consideration. The outcome of a hostile takeover, in the sense that a bid is perceived to be hostile to the management and board or perceived to be hostile to minority shareholders, is contingent on the *choice* of regulation.

This section on takeover regulation presents different theoretical considerations policymakers need to address. It begins by presenting the different considerations relevant to the question of unequal distribution of gains and the work to enable fair price during a corporate control contest. This is built on economic theory, property rights and financial economics. The section then moves on to the legal process of creating a level playing field among corporate actors from different countries with different legal systems and models of corporate governance in order to make it possible to address *cross-border* hostile takeovers. The section ends with a second set of propositions related to the drivers of regulation of and cross-border hostile takeovers

3.3.1 Equal and fair price

The first issue builds on the Manne versus Berle and Means debate on the potential for bids to sometimes involve an unequal division of gains from a transaction and whether this bid-premia instead should be regarded as a corporate asset to be distributed equally among all target shareholders. This addresses the question whether a *fair* price automatically means an *equal* price to all incumbent shareholders, also to be seen as a principal-principal conflict. This line of reasoning is developed from Grossman and Hart (1980), who argue that there are theoretical problems with takeovers connected with the exercise of control. Grossman and Hart claim that the proper management of a common property is a public good to all the owners of the property (here also discussed in section 3.2.3). Monitoring the corporation is a public good as the work of the few benefits the large group of passive minority investors, who as *free riders* can benefit from the active investor's engagement. In a corporation, with a dispersed set of shareholders, the free-rider problem (of passive shareholders) can sometimes be overcome by the use of the takeover bid mechanism, but not always. The free rider problem can also work in the opposite direction, when each small shareholder chooses not to tender in a bid. Each one of the existing shareholders can also choose to free ride on the raider's improvement of the corporation, thereby seriously limiting the raider's profit. To handle that, the raider must increase the price to entice enough shareholders to sell. As a result raids might be unprofitable and socially beneficial takeovers might not occur.

Thus Grossman and Hart (1980) argue against Manne's notion that a corporation with a dispersed owner structure that is not being run in the interest of shareholders will be vulnerable to a takeover bid. Instead Grossman and Hart (1980) analyse exclusionary devices that can be built into the corporate charter to overcome the free riding problem. These include the right to treat minority shareholders differently, for instance forcing them to sell when a raider is in control of 90 per cent, 66 per cent or some other amount of shares. Similarly, strong minority protection is needed, and there might be methods that require 2/3-approval from minority shareholders in the event a raider tries to merge or liquidate the corporation after a successful raid.

Just like Grossman and Hart, Easterbrook and Fischel (1981) argue against the need for an equal price for all shares during a bid. But Easterbrook and Fischel move the perspective from the free-rider issue to investors' preference for utilitarian wealth maximization and the fiduciary principle of corporate law to maximize aggregate gains. In essence, this is a straightforward application of the Pareto principle of welfare economics. As long as both parties feel better in fulfilling the transaction, it will be worth pursuing; thus it should not be necessary for the regulatory authority to strive for equal treatment in corporate control transactions. This reasoning solves part of the Grossman and Hart free rider problem, where equal treatment of different groups of shareholders might lead to bids becoming too expensive for a raider to pursue. Instead Easterbrook and Fischel (1981) justify the sale of control blocks at a premium.

This idea of unequal pricing is taken to heart when Grossman and Hart (1988) argue that an "incomplete contract" and a departure from "one share, one vote" might increase the price as bargaining power is strengthened. Grossman and Hart note that an efficient monitoring of management can only be achieved when a single party becomes large enough to internalize the externalities of collective action, e.g. by making a takeover bid. This suggests that the main impact of a firm's stock voting structure will be in its influence on the market for corporate control, which implies that bidders and blockholders have found an alternative way to solve the control contest by bargaining about price, without involving management. Thus private benefits accruing to a block holder might increase the acquirer's need to pay up, and if the bidder wishes to buy the whole firm all shareholders might profit. As a result, departure from one share-one vote may sometimes increase market value.

Grossman and Hart's (1988) *incomplete contract* approach has also been questioned. Scharfstein (1988) argues that contestability on the market for corporate control should be focused on the disciplinary role a raider can have on management behaviour. Just like Fama and Jensen (1983), Scharfstein views the information gap between the market's perceived value of a company and the raider's perceived value as a prerequisite for a hostile wealth accretive bid to succeed. Only if there exists an information gap will the bidder feels confident that it can increase value more than incumbent management and entice target shareholders to sell off, as they have no means to unlock future value by themselves. As a consequence, the success of a hostile bid is not desirable in itself, but only those bids where there is a true information gap. It might actually be in incumbent shareholders' interest to assure that the corporate management and board agree to sell. Since the target managers run the risk of being replaced after a takeover and thus losing power, prestige and the value of organization-specific human capital, they have incentives to oppose a takeover bid even though shareholders might benefit substantially from acquisitions. If anti-takeover amendments increase the bargaining power of target managers to elicit a higher offer price, they could benefit target shareholders. With this view management should be supported in its fight to resist a bid and take actions to maintain the social welfare mechanism by selling parts, issuing debt and so forth.

The complexity in striking the right balance between a bidder and management during a hostile bid (i.e. the principal-agent conflict), and between different groups of shareholders is taken further by Shleifer and Summers (1988), where the hostile bid mechanism is called wholly into question. They question the common and foundational view that share-price increases for firms involved in hostile takeovers measure efficiency gains from acquisitions. Even if such gains exist, most of the increase in the combined value of the target and the acquirer is likely to come from stakeholder wealth losses, such as declines in value of subcontractors' firm-specific capital or employees' human capital. Thus, the use of event studies (a common statistical method to study abnormal shareholder movement) to gauge wealth creation in takeovers is unjustified. According to Shleifer and Summers (1988) shareholder gains are redistributions from other stakeholders and can in the long run result in deterioration of trust necessary for the functioning of the corporation.

Summing up, this leaves us with the following proposition dealing with the regulatory driver for policymakers:

> *Proposition 3*: An efficient market for corporate control that enables hostile takeovers is a product of law and involves a number of different considerations based on which actors' interests are considered to be most important – the interests of the corporation as interpreted by the incumbent management and board, the target shareholders, the blockholder or the bidding party.

The role of hostile takeovers as a mechanism that both disciplines management and creates value for society must thus ultimately be analysed within the overall governance system. The choice among governance systems and how they might respond to pressures to converge has implications for the development of cross-border hostile bids. These implications for the development of *an (financially) efficient cross-border* hostile takeover market will be addressed in the next sections.

3.3.2 A level playing field

The second part of the section on the regulatory driver deals with the issue of convergence of national governance regimes. During the 1990s, the discussion of the market for corporate control was an important aspect of the European Commission's goal to strengthen Europe's corporate sector vis-à-vis competition from US, China and emerging markets through the formation of European champions. In order to achieve this, the Commission and EU member states pressed for the creation of *a level playing field*, which targeted the deregulation of previously captive markets (for example power generation, telecommunication, and banking) and the opening up the market for cross-border mergers and acquisitions (as expressed in "The plan to move forward" from the Commission, 21 May, 2003). According to Becht (2003, p. 11), "...A European market for corporate control is seen as an integral part of a single market and a major driver of European competitiveness, innovation and growth." Berglöf and Burkart (2003) write that a more vibrant capital market, including hostile takeovers, could help Europe move capital from "sunset to sunrise industries", (cited in Becht et al., 2003, p.11).

In the work to promote a vibrant market for corporate control, an open-minded approach to hostile takeovers as a viable Manne wealth accretive mechanism for society at large fits well into the rationalities governing actors during the 1980s, 1990s and forward, i.e. the era financial capitalism. Specifically institutional investors of various kinds have pushed for the adoption of standard rules and regulations across Europe.[23] As a result, the quest for convergence of corporate governance towards the shareholder model and the development of liquid capital markets enabling a market for corporate control go hand in hand and can be seen as prerequisites for the emergence of a cross-border hostile takeover market in Europe. In different ways, and with various levels of success, the Commission has worked for the promotion of standardized corporate governance models across Europe, harmonisation of corporate law, introduction of codes of governance, transparency requirements, enlarged shareholder rights and the introduction of takeover resolutions.

Two governance features in particular seem to have formed the development of a pan-European regulatory framework for a market for corporate control. These are the conflicting interests that might emerge between the target shareholders as a group and the board of directors and management of the target company (the above mentioned principal-agent conflict) and between the bidding party and different shareholder groups of the target company (i.e. the principal-principal conflict). Both elements are addressed in the Takeover Directive. These relate to anti-

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[23] Coffee (2001) reviews the importance of institutional capital in the modernization of capital markets in France and Germany.

frustration rules or neutrality rules that prevent directors from fending off a bid above a certain level, commonly referred to as the *Board Neutrality Rule*, and the equal treatment of shareholders, including the *Mandatory Bid Rule*. These features are in line with Manne's idea that a market for corporate control is wealth accretive for society while at the same time it targets the difficulty of assuring a Berle and Means equal treatment of shareholders (Easterbrook & Fischel 1981, 1991; Armour & Skeel, 2007). This is illustrated in *Table 1* where both legal devises and theories are presented in relation to the US and UK, two liberal market economies that have settled for different legal interpretations of an efficient market for corporate control. The Commission has generally followed the UK.

Table 1. Theories driving legal devises of (hostile) takeover regulation

		UK	US
Principal-Agent conflict	Instrument	Board Neutrality Rule	Protective Devices
	Theory and Law	Berle and Means (1934)	Director's fiduciary duty to act in the interest of the company Business judgement rule
Principal-Principal conflict	Instrument	Mandatory Bid Rule	Strong minority protection (SEC 1934)
	Theory and Law	London City Code of Takeovers	Manne (1965) Grossman &Hart (1980/88) Easterbrook & Fischel (1981) free rider, utilitarian wealth maximization

Efficient and rational capital markets presuppose that during a bid the board of directors (which in the Anglo-American terminology presumes that directors and management are intertwined) takes a passive role when a takeover-bid is on the table, unable to fight off a hostile bid by other means than through presenting the company in as favourable position as possible. Instead bids – friendly as well as hostile – are addressed, i.e. tendered, directly to incumbent shareholders that are then free to decide to accept the offer. This potential problem is addressed through the Board Neutrality Rule (Article 9 of the EU Takeover Directive).[24] In the UK a board neutrality rule, referred to as a non-frustrative principle, has been in place since the late 1960s (Rule 21 of the UK Takeover Code). It was introduced after a number of incidents in the 1950s and 1960s in which the boards of companies listed on the London Stock Exchange issued shares to fend off uninvited bids. There are different BNRs across European jurisdictions, but the general view has been that the UK represents a sort of "best practise", and it has guided the development of the EU Takeover Directive.

The other feature dominating regulatory development deals with the equal treatment of shareholders, minority shareholder protection and the introduction of a Mandatory Bid Rule (Article 5 of the Takeover Directive).[25] In the Takeover Directive the threshold for a mandatory bid to all shareholders is set at 30 per cent; bidders whose holdings surpass that level are obliged to offer the same price to all shareholders in the target company. The Mandatory Bid Rule is also a British development, dating back to the 1960s and the early days of the *City Panel on Takeovers and Mergers*. "We woz robbed" would be the outcry of the typical British investor (referred to in Hansen, 2003, p. 177) if a dominant shareholder was allowed to sell his or her controlling block at a premium to the market

[24] The issue has been addressed in various EU directives since the middle of the 1990s, including high profile directives such as The Takeover Directive (2004) and Shareholder Rights Directive (2007). Accounts of a Swedish perspective is offered in Skog (2004) and Skog (2007).

[25] A critical account of the Mandatory Bid Rule from a Swedish perspective is offered in Skog (1995). For a critical discussion of the Mandatory Bid Rule, see Davies, Schuster, Van de Walle and de Ghelcke (2010).

price, in the belief that this control premium somehow belongs to all the shareholders, thus reasoning in line with the Berle and Means (1932) view on the control premium as a corporate asset. When the City Panel was set up in 1968 it carried a Mandatory Bid Rule that was limited to acquisitions made from the company itself; it was later expanded in 1972 to cover all acquisitions of effective control.

In a German context, the Mandatory Bid Rule is about exit. It is a way to ensure that minority shareholders can escape the company once control of the company has been centralized to one hand and the company's independence is likely to be compromised or there has been a change in control and a new unknown party has taken control.

The US has taken another direction altogether. In the US the focus has mainly been on dealing with the distribution of takeover gains in line with the free-rider problem (Easterbrook & Fischel, 1981). In the US investors' wealth during a change of corporate control is maximized by a legal rule that permits unequal division of gains, subject to the constraint that no investors be made worse off by the transaction. In some circumstances it might even be preferable to allow for different prices, to ensure that the deal goes through (Easterbrook and Fischel, 1981). The same aspect is taken up in the utilitarian ideas of wealth maximizing (Grossman & Hart, 1980, 1988). These ideas explain why the US has never settled for a Mandatory Bid Rule, demanding instead that a controlling shareholder complies with special rules set up by the SEC. This includes more extensive information requirements by blockholders than in other jurisdictions and sanctions to ensure that minority interests are protected.[26]

Since the heyday of the corporate raiders of the 1980s, US takeover rules have followed the state of Delaware's jurisprudence, allowing corporate management and boards to use defensive tactics provided that they are consistent with the directors fiduciary duties to the company and its stakeholders (e.g. Armour & Skeel, 2007; For a description of the *Busi-*

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[26] The US Securities Exchange Act 1934 requires disclosure of important information by anyone seeking to acquire more than 5 per cent of a company's securities by direct purchase or tender offer.

ness Judgement Rule see sections 5.5 and 6.6). Different kinds of frustrative devices and defence mechanism show up in the US and most Asian stock markets (see Ch. 6 for a more detailed description of takeover regulations in Sweden, the UK, the US and Germany).

In summary, the expectation has been that a common European takeover regulation will bring converged governance regimes through which companies are governed by dispersed sets of shareholders according to the shareholder model on liquid capital markets (and the resulting low capital costs) and that a vibrant market for corporate control open up for hostile takeovers across national European borders (Becht, 2002). Armour (2005) predicts that continental European firms, undergoing a transformation from block holder to dispersed share ownership, a re-listing for example following a private equity exit would find the UK's takeover regime a relatively attractive one. From this the following proposition is formulated:

> *Proposition 4:* A European level playing field enabling cross-border hostile takeovers means giving different groups of shareholders equal treatment, assurance that the board of directors refrain from hindering shareholders from participating in a bid, the abandonment of restrictive arrangements among shareholders and the setting of common standards for the pursuit of a bid.

3.3.3 Critique of the level playing field approach

During the sixth takeover wave, 2004–2008, Europe also experienced a vibrant takeover market (Riskmetrics, 2009). Notably, the number of hostile bids remained few, but that follows lines from the US and the UK, with the mere threat of a hostile bid supposedly being enough to press management to performer better (Scharfstein, 1988; Windolf, 2008). At the same time criticism has been intense, as both the general public and political elites have come to question the societal value of a capital market system that supports (cross-border) hostile takeovers. Parts of the critique against the general push for converging governance mechanisms and thus for facilitating hostile takeovers, lies in the broad variation in corporate governance models, reflecting a variety of capitalism embedded in different local contexts (Coffee, 1991, 1999; Hall & Soskice, 2001).

Several financial theorists have questioned the rationale behind the European regulatory approach to the creation of a level playing field for the market for corporate control and promoting cross-border hostile takeover. The critique targets the European Commission's one-sided preference for British regulation, its focus on the shareholder-value model for governance, with its drive towards dispersed shareholdings as a superior governance model, in contrast to control through block holdings and other defensive mechanisms present all over Europe outside the UK (Becht, 2002; Burkart & Lee, 2007).

Becht (2002), otherwise a strong proponent of shareholder influence (e.g. Becht, Bolton & Röell, 2002), writes that the EU takeover directive, with its then focus on the level playing field and resulting quest for reciprocity in implementing new regulations, would not do much more than increase regulatory complexity and confusion in the current systems of corporate control in Europe. Berglöf and Burkart (2003) warn against introducing pan-European regulations without prior economic analysis, arguing for the importance of understanding what new rules imply for existing ownership and control arrangements in Europe. There are many listed companies that embody good governance, despite having a controlling shareholder protecting them from contestable bids (Franks, Mayer, Volpin & Wagner, 2009).

Goergen, Martynova and Renneboog (2005) argue that similar regulatory changes in corporate governance might have different, sometimes opposite, effects in different countries. More specifically, the implementation of the 13th Directive on Takeovers, whose basic features are largely consistent with UK takeover regulation, might lead to either more dispersed or more concentrated ownership, depending on the initial state of the governance regime in which it is introduced.

Along the same lines Bebchuk and Hamdani (2009) warn of the one-sided European focus on adopting a UK-style investor protection because:

> "The fundamental governance problems of controlled and widely held firms differ significantly, and the effect of many governance arrangements critically hinges on whether the company has a controlling shareholder or not. Arrangements that enhance investor protection in companies without a controlling shareholder are often inconsequential - or even detrimental - to outside investors in companies with a controlling shareholder, and vice versa." (Bebchuk & Hamdani, 2009, p.1263)

Burkart and Panunzi (2006) also address the conflicts present in a governance system with equal treatment of shareholders and a dispersed ownership regime (the principal-principal conflict). Simply put, they conclude that the bargaining power of different shareholder groups cannot be solved in a listed company and as a result the question of equal and perfect distribution of bid-price cannot be entirely solved by private ordering, for this would undermine the efficient dynamics of control allocation and, in turn, efficient separation of ownership and control.

Addressing the heated EU debate on differential voting-rights[27], Burkart and Lee (2007), using Sweden as an example, claim that a concentrated ownership (the dominant model in Continental Europe and the Nordic countries) can be advocated as a simple governance mechanism in order to promote value maximization by firms; either through monitoring or through the alignment of interests. From this perspective, a large controlling shareholder, as noted by Burkart and Lee (2007), might be more efficient as it has the economic incentive to monitor and develop the company. To this can be added that a strict economic approach to corporate governance can show that both product markets and the managerial labour market also provide powerful checks on self-serving rather than shareholder-serving actions on the part of management (e.g. Burkart & Panunzi, 2008).

Distancing himself from the LLSV-literature's preference for UK-US common law, as opposed to civil law of governance, Gilson (2006)

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[27] Ahead of the adoption of the EU Takeover Directive of 2004 there was pressure to stop the system of differential voting shares. The equal treatment of all shareholders is further addressed through the voluntary *Breakthrough Rule* (Article 11 of the Takeover Directive).

argues that Swedish blockholdings and A and B share structure are just as efficient at minimizing agency cost for minority shareholders. Societal pressure appears to be enough to limit abuse such as premium pay for A and B shares during a takeover. In Sweden the premium paid for shares with multiple voting rights during a bid situation has historically been lower than it is in many other countries (Nenova, 2003). Gilson (2006) also claims that hostile takeovers are quite blunt instruments for governance: they are responsive only to certain kinds of governance problems. For example, hostile takeovers may be an efficient device for breaking up inefficient conglomerates that require little internal information to sell off unrelated business, while fixing the problem of a single business may require deep local knowledge of the business that may not be available to an outside owner. The larger premium necessary for success both emphasizes their larger transaction costs and makes them appropriate for only a few very large problems.

Fundamental to the Commission's level playing field approach is the BNR (The principal-agent conflict), yet it too has been subject to criticism from both politicians and academia. In particular Continental European countries with stakeholder governance objected, arguing that there were no level playing field between the member states, and even less between the EU and the US, and as such companies in member states that relied mostly on post-bid defence actions by the board would be prey to hostile bids from abroad.[28] After much controversy the BNR ended up an opt-in-opt out clause in the EU Takeover Directive (Article 9). Davies, Schuster, van de Walle and de Ghelcke (2010) write that the BNR has, in aggregate, likely had an effect opposite to what was expected in the Directive, driving member states more towards protective measures than convergence. Other studies of the BNR claim that it does not work in countries were the minority interest is already taken care of in the corporate law (Gerner-Beuerle, Kershaw & Slinas, 2011).

Much upheaval also preceded the pan-European regulation of a

[28] Hopt (2004/2005/2010) offers a number of accounts on the German objection to the Directive, especially through work in the European Parliament, by the responsible reporter of its Committee on Legal Affairs, Klaus-Heiner Lehne.

Mandatory Bid Rule, implemented on a voluntary basis in most European countries during the 1990s and finally by law through the EU Takeover Directive 2004 (Skog, 1997; Hansen, 2002; Enriques, 2003). As mentioned previously, a mandatory bid, which forces a party which surpass a specific level of control, such as 30 per cent, to offer an equivalent price for all shares, might reduce the incentive to launch takeovers, and thus decrease corporate reconstruction activities that are value accretive for society. At the same time the MBR regime has proven unable to protect minority shareholders in control-seeking transactions, as plenty of loopholes in the regulation make it is easy to circumvent (Enriques, 2003; Grant, Kirchmaier & Kirshner, 2009). To sum up, this section on regulation can be formulated as the following proposition:

> *Proposition 5:* The double quest for both a level European playing field approach for cross-border hostile takeovers and a shareholder governance model reflects political bargaining between member states. The result has been that some countries have a takeover regulation that is more supportive of liquid free-market capitalism, while others maintain corporate law that includes protective devices. This is reflected in an uneven playing field among corporate actors across Europe.

With this, the section moves to the third and final building block of theoretical drivers for policy makers in the creation of a level playing field for a European market for corporate control – financial capitalism and the tendency for short-termism among institutional investors.

3.4 Driver 3: Institutional investors and short-termism

3.4.1 Institutional investors in financial capitalism

Ownership is important. It is the owners that have the power (i.e. voting rights) to push for value creation within the legal entity of the listed corporation. It is also owners who are decisive for the emergence of a market for corporate control by virtue of their right to buy or sell stocks on liquid capital markets. There exists a range of owner types – stemming from founding entrepreneurs, banks, capitalists and different kinds of institutional investors. They all have different rationales for their ownership, both in their roles as active owners and in their choice of investment horizon. The latter group, institutional investors, has been the dominant actor on the stock markets in the era of financial capitalism (see for e.g. Hawley & Williams, 1997, 2007).[29]

Institutional investors are nothing new per se. Trusts, life-insurance companies and foundations have been around for well over a century. Since the early 1980s these institutional investors have been complemented by a number of retail funds, pension funds, activists and hedge funds as well as state-owned sovereign-wealth funds and state owned sovereign pension funds (Charkham & Simpson, 1999; Gourevitch & Shinn, 2006; Monks & Minnow, 2008). As a group these new institutional investors have taken a dominant role in global capital markets. In the UK personal direct investment was responsible for over 60 per cent of the shares in the late 1950s with institutions controlling less than 20 per cent in total. In the 1980s the balance had been all but reversed (Charkham & Simpson, 1999). In 2006 private investors' share of the UK stock market share was down to 11 per cent. In 1963, foreign institutional investors owned 7 per cent of UK shares, but by 2006 the share was 46 per cent (Mallin, 2007, p. 77).

The US followed the same trend, albeit later and without true dominance of the insurance industry. In the US individuals owned 90 per cent of the listed stocks in the 1950s, a presence that had been reduced to 25 per cent in 2004 (Armour & Skeel, 2007). The presence of institutional investors went the opposite direction (partly as a result of the Erisa-legislation, 1974)[30]. The percentage of equity in the thousand largest US companies controlled by institutions went from 25 per cent in early

[29] An academic overview of the role of institutional investors on the Swedish capital market is offered in Nachemson-Ekwall (2012a).

[30] The Employee Retirement Income Security Act of 1974 (Erisa).

1970s, to almost 47 per cent in 1987 and around 59 per cent in 1996 (The Conference Board, 1997).

The German economy had been dominated by a relatively small number of key players, family owners (*Gr:* "Mittelstand"), companies bound in networks of crossholdings and banks (a constellation sometimes known as *Deutschland AG*. Together they accounted for over two thirds of German share ownership (Lannoo, 1999, p. 277). But change has occurred, and in Germany the presence of institutional investors increased from nine per cent in 1960 to 22 per cent in 1990 and foreign investors rose from six to 14 per cent in the same period (Lannoo, 1999). The trend toward a growing presence of institutional investors has also been seen in the rest of Europe. In 2005, foreign investors, which could be presumed to be institutional investors of various kinds, owned 33 per cent of all stocks in Europe. Pension funds owned 24 per cent, households 15 per cent and non-financial institutions held 16 per cent (Federation of European Securities Exchanges, FESE, 2007). This trend has also been very clear in Sweden. In 1990 institutional investors owned 25 per cent of the market capitalization on the Stockholm Stock Exchange. In 2011 the group owned over 50 per cent (SCB, 2012; also Ch. 6.2 and *Table 7*).

As an investor type this new group of institutional actors share some common characteristics (Hawley & Williams, 1997, 2007). They often invest assets that have emerged from more or less the same source – collective savings. They often act as intermediaries and fiduciaries for distant investors, which could be a future retiree or a long-term, private retail saver. Hawley and Williams have described this as the emergence of *fiduciary capitalism*, in the meaning that most citizens have become indirect holders of investments in almost all listed companies. This also means that the performance of their portfolio is dependent on the well being of an overall economy. Black (1998) and Romano (2001) highlight that many mutual fund managers hold stakes in companies for which they also carry pension-fund mandates, which invites conflicts of interests. The same goes for pension funds linked to unions and employees. Many public pension funds are under the influence of politicians, who are elected by constituencies whose interests are not identical to those of the pension fund beneficiaries.

A number of studies have been conducted trying to estimate the performance of these institutional investors. A survey presented in Bauer, Cremers and Frehen (2010) shows inconclusive results. The lack of comprehensive return, benchmark and cost data and possible self-reporting biases have induced a broad diversity of conclusions on pension fund performance and costs. Studies of mutual fund performance show that after expenses and trading costs, mutual funds perform on average slightly worse than benchmark index (Bauer et al. 2010). Shareholder activism in the US has generally not been able to trace exceptional performance either (Romano, 2001). Becht, Frank, Mayor and Rossi (2008) study shareholder activism in the UK through the focused Hermes fund, HUKFF, over the period 1998–2004. Becht et al. trace annual raw returns net of fees of 8.2% and abnormal returns net of fees of 4.9% a year against the FTSE All-Share Index over the period 1998–2004. Becht et al. estimate that around 90 per cent of such fund returns arise due to activist outcomes. Overall these studies say little about the effect of the value-building process in the specific company on a case-to-case basis, which is the focus here. They also give little guidance on possible reasons for the lack of performance.

3.4.2 Portfolio theory and shareholder value

As mediators, fund managers are obliged to submit to different kinds of regulations. There are general regulations related to responsibilities and obligations that apply to all actors in the pensions and savings industry. There are rules that reflect financial theories of portfolio management. There are regulations reflecting political and ideological preferences. *Quantitative rules* regulate asset-allocation between different asset-classes, countries, or exposure to certain companies. There are also *qualitative rules* that direct decisions related to prudence, loyalty and impartiality encompassed in the *prudent person principle* and part of the EC's occupational pension directive (*Sw:* "aktsamhetsprincipen"; Björkmo, 2009; The Directive

2003/41/EG). These rules frame modern asset management. Since the 1980s prudent asset management has been synonymous with risk-allocation and diversification in accordance with the principles that follow from the financial theory of efficient and well functioning capital markets presented through the Fama (1983) efficient market hypothesis (also Ch. 2.4). The result has been that many investment managers have both many stocks in their portfolio, often over a hundred different investments, and very small shareholdings in each of them. These ideas of risk-allocation and prudence have been shown to have some limitations, and this became apparent after the financial crisis of 2008 (Franzén, 2009; Johnson, 2011; Hawley, 2011):[31]

- They presuppose that the market actors are rational investors, fully informed and that occasional mispricing of shares is immediately corrected and share price returns to their correct value. In reality these institutional investors are prone to follow investment strategies set by others, resulting in herding behaviour.

- Many institutional investors follow indices rather than specific companies and therefore lack the ability to participate in the value accretive governance process. This follows from the way the investment managers are rewarded, through benchmarks, asset volume under management and short-term incentive programs.

- The portfolio-allocation model is dependent on someone else being well informed. But if more or less everyone is prone to herding behaviour and following index, the outcome will instead be asset bubbles that eventually burst at a great cost for society.

Thus, this group of new institutional investors have for a number of reasons had a preference towards liquidity, i.e. ability to buy and sell, and

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[31] An overview on research of institutional investors and short-termism is also offered in Heineman (2011).

the shareholder model for governance.

In a governance environment were shareholders have legal means to influence board composition the preference by institutional investors (for liquidity and shareholder value) has certain implications for different stakeholders (Samuelsson, 2005; Aglietta & Rebérioux, 2005). An empirical study by Bushee (1998) based on US-level market data claims that increased institutional ownership is linked to increased myopic behaviour whereby managers underinvest in long-term intangible projects (R & D, advertising and employee training) in order to meet short-term goals. Franzén (2009) looks at the Swedish market with its dominance of institutional investors to make a case that the behaviour of herding and index-tracking investment policy may potentially be especially harmful. Franzén argues that it is illogical for equity investors with long-term obligations such as a (Swedish) national pension fund, to demand 15–20 per cent return on equity from the companies they invest in when market rate of return settles for 8-10 per cent and the GDP growth of the overall economy stops at three per cent. The result will be a lack of investment in long-term value accretive projects. Franzén (2009) suggests that this might be troubling, not only for the individual company's chances of growing, but also for society.

Given the discussion above, one can ask whether financial capitalism might promote a tendency for *short-termism* among institutional investors. As defined by the CFA Institute in 2006, short-termism refers to the excessive focus of some corporate leaders, investors and analysts on short-term earnings guidance coupled with a lack of attention to the strategy, fundamentals and conventional approaches to real value creation, which is a long-term process. The combination of these elements can upset the balance in the value for market participants, undermine the market's credibility and discourage long-term value creation and investment (*Breaking the short-term cycle*, p.1, Business Roundtable of Corporate Ethics and CFA Institute, 2006). Researchers tend to agree on the definition of the concept of short-termism, but, even after the global financial crash of 2008, it is hard to establish whether short-term decisions are actually detrimental to long-term value creation in much the same way as it is impossible to know ex-ante whether a hostile bid is value destructive or accretive. Jackson and Petraki (2011) address this dilemma by referring short-termism as "a social process caused by a self-reinforcing and dynamic calibration (shortening) of time horizons produced through the interactions between shareholders and managers, and amplified by several roles played by gatekeepers in mediating these relationships" (p.11). This shortening of time-horizons is for example produced by the interaction between on the one hand shareholders – pension funds, private equity, hedge funds – and on the other managers. Short-termist behaviour is supported by activities from gatekeepers mediating these relationships such as securities analysts, credit-rating agencies, auditors and the media (Coffee, 2006). As part of this social process, short-term wealth creation through maximisation of stock market price seems to be the yardstick of success. Corporate leaders often focus more on quarterly earnings to meet the quarterly earnings expectations of the analyst community.

3.4.3 Critique of institutional investors and short-termism

Johnson and de Graaf (2009) make a case for expanded definitions of duty for pension fund fiduciaries in this short-termist environment, as shown in *Table 2*. A number of actors are involved in the decision-making with different and sometimes contradictory agendas. The agency conflict between the ultimate shareholder (the principal), for example a future retiree, and the corporate management (as final agent) is here illustrated as a chain of agents acting as mediating actors, all with a different interpretation of their fiduciary role, personal goals and investment horizons. Stuides of the work by financial executives and managers highlight the dilemma. A survey by Graham, Harvey & Rajgopal, 2005; Price WaterhouseCoopers (2011) show that a great majority of the CFOs and CEOs would reject a project based on the fact that in the short-term it may take the quarterly earnings below the consensus expectations or they would give up economic value to smooth earnings.

Table 2. Stakeholders in the pension-fund industry

Stakeholder	Horizon	Agent Problem	General Description
Participants/ Beneficiaries	30+years	Often have/exercise little control over the contributions or investments.	Are neither involved nor knowledgeable, which leads to mistrust at times of financial distress.
Trustees of Governing Board	4 to 6 years	Often union, employee or government representative with independent representatives in some countries. They are in a position for a limited time and typically have little financial or investment background.	May not have necessary skills and are sometimes driven by other interests (e.g. employers and employee representatives might also negotiate wage agreements), financial incentives are usually small.
Investment Managers	1 year	Work on short-time bonuses with clients who often evaluate performance over 1-3 years.	Are incentivized by fees related to assets under management and are evaluated relative to benchmarks, which might not reflect pension-funding needs.
Managers of Companies	3 to 12 months	Only know a few vocal or active investors. In many countries less than 30 percent vote by proxy. Little interaction.	Feel hunted and pressured to deliver quarterly returns by investors they do not know; are influenced by incentives based on stock price.

Johnson & de Graaf (2009)

Empirical evidence and estimates suggest that projects are very often rejected due to the use of higher discounting rate for future cash flows. For instance, a 10-year project is often discounted at 15-year rate, making its net present value negative. Thus the definition of what is long-term in investor outlooks has shortened considerably over time, creating myopic behaviour and a preference for short-term payback rather than long-term value creation (Haldane & Davies, 2011). This makes short-termism a public policy issue:

> "Short-termism is both statistically and economically significant in capital markets. It appears also to be rising. In the UK and US, cash flow 5 years

> ahead are discounted at rates more appropriate 8 or more years hence; 10 year ahead cash flows are valued as if 16 or more years ahead. The long is short. Investment choice, like other life choices, is being re-tuned to a shorter wavelength… This is a market failure. It would tend to result in investment projects being too low and in long-duration projects suffering disproportionally. This might include projects with high built or sunk costs, including infrastructure and high-tech investments. These projects are often felt to yield the higher long-term (private and social) returns and hence often offer the biggest boost for future growth." (Haldane & Davies, 2011, p.11)

Short-termism also seems to be decisive when institutional investors participate in a corporate control contest, in the sense that they are for example likely to act as sellers in a bid situation and also in a hostile bid-situation (Minnow & Monks, 2008; Aglietta & Reberioux, 2005; Kallifatides, Nachemson-Ekwall & Sjöstrand, 2010). At the same time hostile takeovers and the market for corporate control are specific mechanisms of financial capitalism that, as brought forth in Windolf (2008), seem to transfer the operational logic of the market to real economics (a financilization of companies). This is conceptualized by Kallifatides et al. (2010), who claim that financial capitalism, with its tendency to rely on external markets for governance, represents a break from industrial capitalism, which had its governance flow revolving around the internal flow of goods, capital and contracts. One could claim that financial capitalism — with its domination of institutional investors — has brought control and governance processes to the forefront and placed managerial activities in the background. Huse (2007) claims that this is the result of shareholder value having become the dominant ideology of corporate boards in financial capitalism. Directors have, as explained above (section 2.3.2), a broader responsibility to multiple stakeholders than the mere promotion of shareholder value (short-term). This approach builds on the critique of the shareholder-value model as the "superior" catalyst for governance (Brodin et al. 2000; Lazonick & O'Sullivan, 2000; West, 2009). The critique brought forth here also encompasses part of the scepticism to the hostile takeover as a mechanism for the creation of an efficient market of corporate control (see e.g. Gilson, 2005; here in Ch. 3.3.3). Its simply does not seem to work as expected on deregulated capital markets with active institutional investors (Reberioux, 2002; Aglietta & Reberioux, 2005; Wymeersch, 2008).

Empirical studies show that it is not always the question of long-term value creation that is the decisive factor when ownership is decided on a hostile takeover; what is decisive is which *coalition of actors best masters the playing-field* (Jackson & Miyajima, 2008; Kallifatides et al. 2010). Indications of this distortion of the power play between actors on the market for corporate control appeared to be present in European countries during the sixth takeover wave. The activities of institutional investors during a cross-border deal appear also to be influenced by regulations (such as rules on domestic asset allocation), liquidity preferences (rules limiting the ability to invest in non-listed companies) as well as a general exposure to a certain index composition (Ferreira, Massa & Matos, 2009; Kallifatides et al. 2010).

The presence of short-termism in a given stock market or in connection to a specific company seems to depend on what kind of features dominate the national governance model, how it has evolved through a controlling blockholder structure or a dispersed ownership structure, and how the system has responded to importing new regulations (through e.g. a EU directive). The question thus becomes how new investor-owners interpret their responsibility and mandate. For example, a national corporate governance system built on controlling shareholdings through the usage of multiple voting rights, trading of these block-holdings to actors not subscribing to this regime, (its codes, norms and history) might invite abuse of minority shareholder-rights and thus force these incumbent shareholders to sell off shares at a lower price.[32] At the same time, blockholders, as ultimate owners governed by a financial shareholder perspective, might act short-term in order to gain legitimacy with the community of globally active pension funds. This might for example be the case if the block holder is a listed investment company or a retail

[32] The issue is of course relevant from a Swedish governance perspective and is discussed in Burkart and Lee (2007). Volkswagen's actions in Scania 2010 against the minority shareholders are recent examples. The Swedish Shareholders Association has historically worked hard to protect minority shareholders.

fund with an index-tracking investment policy.[33] These conflicts are illustrated in Table 3 where the different investment horizons and the goals of managers and shareholders meet in four different arenas. Only one field, where long-term managers and long-term investors meet (in the fourth square), enables sustainable value creation.

Table 3. Time-horizon of governance and sustainable corporate value creation

	Manager preference Short	Long
Shareholder preference		
Short	"Short-termism"	Agency Conflict Long-term managers pressured by short-term investors
Long	Agency Conflict Long-term investing undermined by short-term opportunism of managers	"The Sustainable Company"

Possible danger with this short-termism is being discussed globally. When *International Corporate Governance Network*, ICGN,[34] revised its Corporate Governance Principles in 2009, the first lines specifically stated: "The objective of companies is to generate sustainable shareholder value over the long-term." This highlights the fact that a group of institutional investors might, just like other investors, be active or passive investors as

[33] Fiduciary obligations to policyholders and ultimate beneficiaries are discussed in the European Commissions Green Paper on Corporate Governance, April 2011.
[34] The ICGN is a global membership organisation of over 500 leaders in corporate governance based in 50 countries with the aim to raise standards of corporate governance worldwide. It represents funds under management of around US $18 trillion.

well as long-term or short-term oriented in their investment approach, and that a regulatory framework can be used to promote different kinds of behaviour.

This section on institutional investors in financial capitalism can be summarized in the following claim:

> *Proposition 6:* Regulations, norms and incentives have made institutional investors such as pension funds focus on trading, liquidity and short-term stock-performance, thus limiting their role as corporate governors. This might hamper long-term value creation of companies and distort outcome during a cross-border hostile takeover process.

3.5 An institutional perspective

Drawing on financial economics, management theory and law to build a theory that explains the drivers for policymakers to enable cross-border hostile takeovers, a complex web of considerations emerges. In order to provide a complete picture the reasoning here is extended to include a framework built on institutionalism (Section 2.2). Here this is developed with specific reference to Aguilera and Jackson (2003) and Aguilera et al. (2007).

3.5.1 Actor-centred approach

Institutionally oriented academics share and express the feeling that despite the benefits attached to financially efficient corporate governance and increasing pressures to enhance it, changing governance systems is not an easy task because governance practices are embedded in the broader institutional environment (Hollingsworth & Boyer, 1999; Aoki, 2001). Once different national governance systems were understood as more than just stations on the road to convergence, comparative scholars also began to treat institutional differences as having competitive consequences. Competition was not based solely upon products, but also upon governance systems. For example, Aoki (2001) argues that Japanese lean production was inextricably linked to the Japanese governance system in which main-bank contingent monitoring and cross-shareholdings protected the promise of lifetime employment by shielding managers and workers from shareholder demands, but disciplined both groups in the event of poor performance. Thus the question will be whether we can expect a formal convergence of legal rules, as Hansmann and Kraakman (2001) argue has largely been achieved, or, as Gilson (2000) argues, is merely a functional convergence that operates behind a wall of local institutions.

A more institutional approach would point to the idea that both actors and their goal are not to be seen as a given, but instead as constructed by the positions they play in society (Aguilera & Jackson, 2003). This has implication for importing new takeover regulations or governance mechanisms from one country to another. A strong advocate of convergence to Anglo-American shareholder ideals, Roe (2003) claims that political determinants primarily explain differences in ownership concentration in Europe. According to Roe a shift to open capital markets across Europe (i.e. the opening of national borders to create a level playing field) would bring forth pressure for support of dispersed shareholdership and challenge domestic policymakers in the promotion of a domestic legal framework supporting this. In this context a parallel establishment of a pan European financial capitalism would represent both opportunities and challenges. From the Roe perspective this is an opportunity because it could enhance economic growth within the European Union. It is also a challenge because it forces Europeans to weight the pros and cons of their own differing systems.

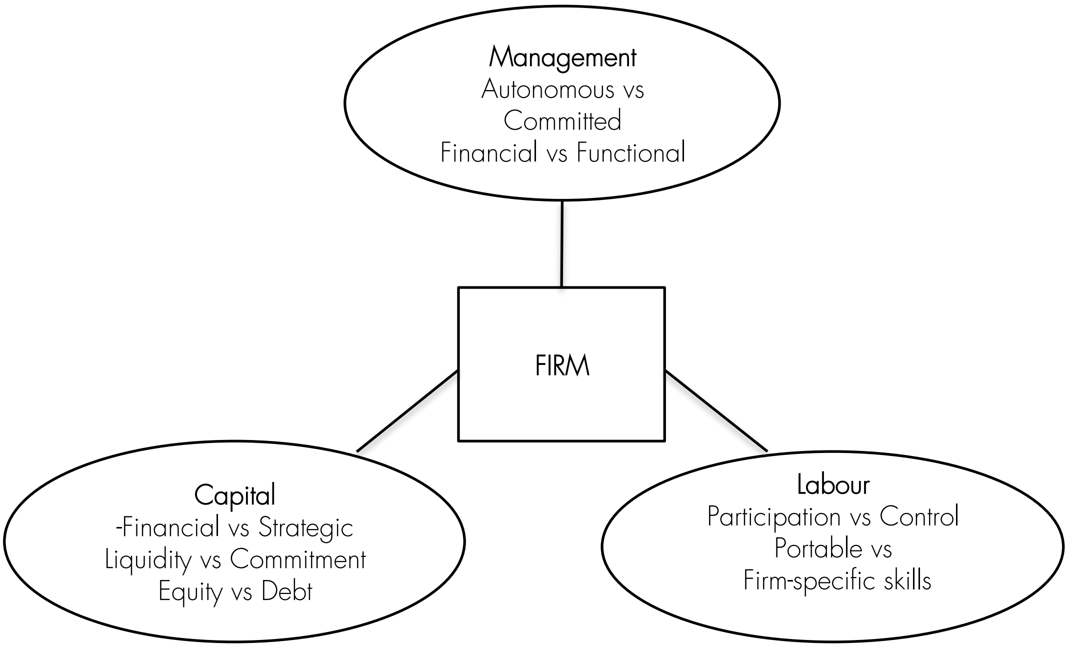
Using the idea of institutional complementarities, Aoki (2001, p. 31) writes that: “institutions in the past and in the future are mutually interlinked in a complex manner”. Institutions generated endogenously at one point of time may at a later period interact with agents in a different way than what was the original intention of the policy makers. Pointing to this problem, Fligstein and Choo (2005, p. 80) write: “The importation of another country’s corporate governance institutions is not likely to work unless the entire system is borrowed or the borrowed system fits with what already exists in a given society."

Many academics have also begun to question the finance literature's approach to investors as a homogenous group with common preferences and as concerned only with maximizing shareholder value (Aglietta & Reberioux, 2005; Jackson, 2011). As stated previously, shareholders differ in their wish to maximize shareholder value depending upon what they represent: a bank, a family, another corporate owner, a private equity firm, a state or sovereign wealth-fund. There are also variations within each group.

This question is developed further in Gourevitch and Shinn (2006), who highlight that economic systems change over time and respond to new actors and coalitions of actors that enter the scene. Describing the effects of the emergence of institutional investors such as pension funds as driver of change in corporate governance, Gourevitch and Shinn argue that institutional investors will form coalitions with management, other minority-holders or blockholders to influence change in the direction of transparent shareholder-value governance. However, Gourevitch and Shinn fail to include hedge funds, activist funds, sovereign-wealth funds and the like in their analysis. Neither do they discuss the shareholder-value mechanism, herding and the resulting preference for short-termism among institutional investors or the extreme focus on index tracking by portfolio managers. Equally important is an understanding of what roles different actors play during a hostile takeover fight in financial capitalism. These include middlemen such as investment banks, journalists, lawyers, auditors and analysts (Coffee, 2006; Kallifatides, Nachemson-Ekwall & Sjöstrand, 2010).

Along these lines there are a growing number of academics that question the ideas governing the creation of an efficient market for takeovers, especially cross-border hostile takeovers. In that vein I build on Aguilera and Jackson's (2003) "actor-centred" institutional approach to understanding diverging corporate governance (shown in *Figure 5*).

Figure 5. Dimensions of corporate governance



Aguilera & Jackson (2003)

Picturing three dimensions of corporate governance – capital, management and labour - Aguilera and Jackson (2003) stress the interplay of institutions and firm-level actors and argues for a further integration of interdependencies in the convergence debate. The three dimensions demonstrate how agency theory fails to explore sufficiently how corporate governance is shaped by institutional embeddedness. The best way to analyse converging corporate-governance regimes is, accordingly, to present an analytical framework that:

- Factors in a country's property rights, financial system and inter-firm networks that shape the role of capital.
- Includes how a country's representation rights, union organization and skill formation influence the role of labour.

- Explains how a country's management ideology and career patterns affect the role of management.

In the Aguilera and Jackson (2003) framework convergence in governance will rather result in hybridization were different coalitions of power spheres within the national governance elites adapt in their own ways to external forces.

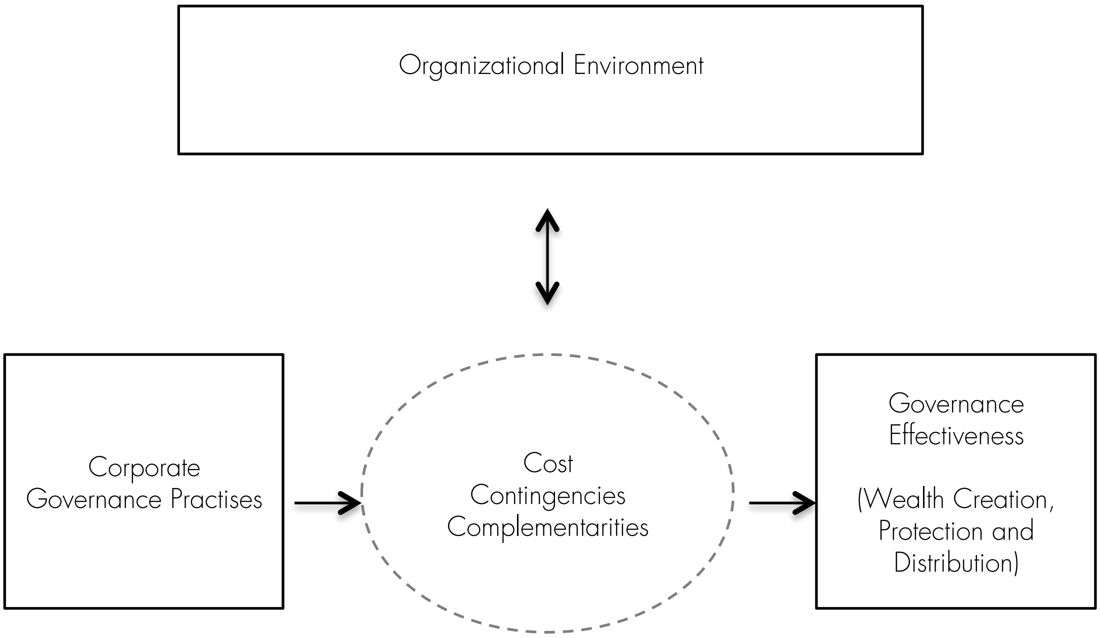
3.5.2 "Open systems" approach

I also follow calls from Aguilera, Filatotchev, Gospel and Jackson (2007) to account for how interdependences between the organization and diverse environments lead to variations in the effectiveness of different governance practises. Here this means the governance practices relevant to takeovers, specifically hostile takeovers and cross-border hostile takeovers.

Aguilera et al. (2007) propose an analytical framework based on an "open systems" approach to organizations (shown in *Figure 6*) which examines these organizational interdependencies in terms of "costs, contingencies, and complementarities" of different corporate governance practices. This includes both different organizational environments (Thompson, 1967; Scott, 2003) and a stakeholder perspective (Freeman, 1984).

Costs refer to the value of inputs to corporate governance, such as compliance with existing regulations or opportunity costs of managing relations with institutional investors. *Contingencies* refer to how corporate governance relates to variations in internal and external strategic resources that shape a firm's interdependence with market, sectorial, regulatory or institutional environments. *Complementarities* refer to the overall bundles of practices that are aligned to mutually enhance effective corporate governance. Aguilera et al. (2007) note that the notions of contingencies and complementarities may be interrelated, but still claim it useful to separate them as two independent theoretical constructs. In the framework, contingencies impact the effectiveness of a particular corporate-governance practice, *ceteris paribus*, whereas complementarities describe interactions among multiple practices notwithstanding the firm's contingencies.

Figure 6. Organization and corporate governance



Aguilera et al. 2007

According to Aguilera et al:

> "Even though these three constructs may not comprehensively account for the complexity of interdependence between organizations and their environments, we believe that costs, contingencies, and complementarities are useful conceptual tools to analyse why effective corporate governance can be reached through different paths and nonlinear trajectories…"(Aguilera et al. 2007, p. 5)

The inclusion of interdependencies is, according to Jackson and Miyjami (2007), especially important in understanding the effects of importing different rules and regulations and the reasons why convergence does not always generate the expected outcome. Jackson and Miyjami (2007) compare the characteristics of mergers and acquisitions in 1991–2005 across five countries: Japan, France, Germany, the UK and the USA. Despite some convergence toward increasing levels of M&A activity Jackson & Miyjami find important differences in the characteristics of M&A transactions that reflect institutional differences within different national "varieties of capitalism". The paper claims that there exist systematic differences between what Hall and Soskice (2001) call liberal market economies (the UK and the US) and coordinated market economies (such as Japan, France, and Germany) across a wide range of deal characteristics: takeover bids, the size of stakes purchased, the prior stakes held, the use of private negotiation, degree of hostility, and takeover premium. In line with theories of social embeddedness of markets (Granovetter, 1985), Jackson and Miyjami show that countries with "coordinated" market economies feature M&A activities that reflect a greater "coordination" of transactions through ongoing business relations. As such, a market for corporate control does not necessary entails a convergence of national business systems but a pattern of change influenced by strong continuities.

Using statistics from 538 hostile takeover attempts (successful and unsuccessful) in the US, the UK, France, Germany and Japan, Jackson and Petraki (2007) show that while some target firms were clearly performing badly, these cases were not typical of the majority of target firms in hostile bids in any country, which suggests that there might be institutional explanations for hostile takeovers rather than some agency theory of efficiency. Here I would claim that in an environment of a hostile cross-border takeover, where the constituencies involved follow different regulatory regimes, there might also be indications of regulatory arbitrage (Kallifatides, Nachemson-Ekwall & Sjöstrand, 2010). Even worse, in an environment were constituents protected by controlling devices are free to act, also cross-border, the less-protected target will not only be acquired, but there will be fewer possible actors overall than in a hypothetical efficient market for corporate control, which may reduce possible long-term welfare creation for society (Haldane & Davies, 2011). This reasoning suggests that the market for corporate control might only work one way – big companies buy smaller ones, and not vice versa, so big firms face a shorter list of probable predators and challengers to management (Martynova & Renneboog, 2006; Aguilera et al. 2007).

Aguilera and Jackson (2003) note that neither actors nor their goals are to be seen as given, but instead constructed by the position they play in society and also in relation to regulatory space (see also section 2.2). The concept of regulatory space can, according to Crouch (1986) and Hancher and Moran (1989), be used to understand the difference between the US tradition of regulating everything, as the government is seen as a weak party, in contrast to the European regulating approach made up of bargaining between different interest groups. Hancher and Moran (1989) play an important role in Scott (2001), which develops a framework for changing corporate governance practises. Scott refers to research that has found that the national legal system is often a secondary rather than a primary focus for regulation, thus implying that it is necessary to look at activities by many different actors before being able to fully grasp a regulatory context. As an aspect of understanding how the regulatory system works, Scott refers to the presence of professionals regulated so as to be able to act in the interest of a regulatory body. These "gatekeepers" can be accountants, medical doctors and so forth (Coffee, 2006).

Scott (2001) uses the idea of regulatory space to discuss institutional design in the EC context, which offers a broad spectrum of actors involved in bargaining, regulatory capture and other power processes. Scott claims, like Hancher and Moran previously, that large firms are especially well equipped to involve themselves in regulatory processes, concluding that this has effects on the EU/UK idea of self-regulation. Striking the right balance between self-regulation and legislation has also been an important discussion in forming the EU internal market and explains many of the complications in the work of converging different capitalistic systems in Europe. This approach is also consistent with the description by Fligstein (2001) and Roe (2003) of the power play between shareholders, managers and employees and how these are influenced by social, economic and cultural factors.

Leaning on institutionalism the last proposition related to theoretical drivers for policymakers of a market for cross-border hostile takeovers is formulated as follows:

> *Proposition 7*: The convergence of national models of governance to one "best system" has not happened as expected because national governance systems are contingent on past experience and corporate law as well as culture and social embeddedness.

3.6 Conclusion

The theoretical drivers for European policy makers in their work with *levelling the playing field* among corporate actors across Europe, with the overarching aim of creating a financially efficient market for corporate control, emerges as a multidimensional process. This chapter focused on three drivers as especially relevant for the outcome of a cross-border hostile-takeover process. First is the quest for a coherent system of corporate governance where shareholder value emerges as the "best model". This quest has led European policymakers to push both "soft" and "hard" law in a direction away from stakeholder-value principles to shareholder-value principles. An integration of financial economics, liquid capital markets and agency theory play a central role in this process.

The second theoretical driver relates to this building of a common and coherent regulatory framework that supports a cross-border market for corporate control. This work highlights a number of differences between US and UK approaches to the market for corporate control in general and hostile takeovers specifically. The two countries are to be seen as some of the most liberal and most shareholder-friendly economies, with highly active markets for corporate control and propensity for shareholder value. Yet, they express different ways of dealing with two major agency problems during a takeover process. On the one hand it is the role of management vis-à-vis shareholders of the target company (the principal-agent conflict). This problem relates to firms with dispersed shareholders in a Berle and Means (1932) sense. The US market allows management to utilize a number of protective measures to fend off a hostile bid, but the UK regulations restrict management and the board. The other agency conflict relates to the role of the bidding party vis-à-vis target investors (the principal-principal conflict). This problem relates to a situation with either an incumbent controlling block holder acting during a contest for corporate control or a bidding party buying a block of shares and thus emerging with control. The UK solves this latter agency conflict by forcing a bidder or controlling shareholder, which gains control of more than 30 per cent of shares or votes, to offer a bid to all other shareholders. The US has instead settled for a legal framework focused on minority shareholder protection. The EU Takeover directive has leaned towards the UK when addressing both problems and introduced a Board Neutrality Rule to deal with the former conflict and a Mandatory Bid Rule to deal with the latter conflict.

The third theoretical policy driver reflects the role of institutional investors such as pension and retail funds, a group that has emerged as dominant actors on capital markets in modern financial capitalism. Regulated and incentivised to invest according to portfolio theory and evaluated in relation to different indexes they have emerged with a rather haphazard investment style. This appears to influence the outcome of a cross-border hostile bid process in two ways. One relates to index tracking, leading to short-term selling when the stocks of a target company rise in relation to other stocks in the index. Another issue is related to liquidity where many institutional investors are required by regulation to invest in listed companies, often also included in a specific index. When the free float is reduced, for example when a bidder gets control of a large portion of the company's stocks, they will automatically sell off their position.

An institutional perspective on the three drivers for a cross-border hostile takeover process identifies plenty of theoretical arguments supporting the view that nations have developed different systems of corporate governance to be able to deal with national environments in a cohesive and predictable way. Thus, it is not possible simply to claim that there is one corporate governance system that is superior, at least not if the aim is to create an efficient market for corporate control. Rather, simply importing one mechanism to a country, i.e. as a result of a EU directive or pressure from regulated institutional investors, might destabilize the national governance system making it dysfunctional. Pacces (2010) writes that there is a growing tendency to question whether convergence actually is taking place, thus revealing scepticism congruent with much of the literature presented in this chapter.

In the chapter I have developed seven propositions related to the theoretical drivers for a cross-border hostile takeovers process. When I frame theses in institutional theory, borrowing ideas from Aguilera and Jackson (2003) and Aguilera et al. (2007) the seven propositions are transformed to three hypotheses:

> *Hypothesis 1:* A corporate governance model contingent on ownership governance has difficulties in its quest to balance the value accretive strategy of directors and executive management with financial capitalism's one-sided preference for (current) shareholder value and liquidity over more stakeholder oriented governance models.

> *Hypothesis 2:* Institutional investors investing according to portfolio theory and with a preference for shareholder-value governance may push corporate directors and management towards short-term strategies and facilitate cross-border hostile sell-outs.

> *Hypothesis 3:* Open and liquid capital markets with globally active investors investing in domestic capital markets with diverging corporate governance systems enable arbitrage, both regulatory and morally.

Taken together these three hypotheses indicate that the outcome of a cross-border hostile takeover process may not reflect a well functioning and financially efficient market for corporate control. If this is the case, it will have implication for the European regulatory push for construction of a level playing field among actors. To study this construct in more detail I proceed by presenting a specific national setting, that of Sweden. I present three case studies of cross-border hostile takeovers and a description of the development of the Swedish takeover rules. In doing this I focus on dynamic factors that demonstrates the interplay of actors' behaviour in financial capitalism with that era's susceptibility to short-termism and enabling of regulatory arbitrage and moral arbitrage.

Chapter 4

Method

The overarching goal of this dissertation is to study the making (and shaping) of a market for corporate control. I wish to study its actors, processes and institutions. I focus on the corporation and how the board's role is influenced by takeover regulations in financial capitalism. From this I have formulated my research question:

> "How can we understand the idea of a well functioning market for corporate control and the effects of regulatory convergence of different corporate governance regimes (in Europe) in financial capitalism?"

Beyond the theoretical exposition of the field, the dissertation evolves through six studies *(Table 4)* of which four are case studies. These cover:

- The Swedish corporate governance system and institutional background (Ch. 5).
- The Swedish market for corporate control and takeover regulation and its institutional background (Ch. 6).
- The cross-border hostile bid on Skandia (Case 1 in Ch. 7).
- The PE hostile bid on Capio (Case 2 in Ch. 7).
- The cross-border hostile bid on Scania (Case 3 in Ch. 7).
- The revised takeover regulations 2009 (Case 4 in Ch. 8).

The first two studies are background descriptions based on literature, including comparative material from other nations. These two studies are to be read as constituting the institutional setting of the three case studies of cross-border hostile takeovers. The sixth case study constitutes both a description and a comparative analysis built on knowledge developed both through an in-depth analysis of the 2009 revision of the Swedish takeover regulations and the previous three case studies.

Table 4. Four case studies

Dates of research	Case study	Main empirics studied	Time period covered
2007-2009	Skandia	Narrative, multi study with 75 persons interviewed many times	2004-2006
2010	Capio	Narrative, media-reporting checked against facts from 10 persons	2006
2010-2011	Scania	Historical account built on public sources, media-reporting, and legal documents	1999–2011
2011	Takeover regulation (2009)	Legal documents, public reports and academic texts	2007–2010

4.1 The epistemological perspective

Distancing myself from textbook economics and finance theory with ideas of efficient capital markets and rational actors, I rely on sociology and institutionalism to find out how takeover regulations have developed and what forces influence the outcome of a cross-border hostile takeover process. This means that I base this dissertation in a socioeconomic tradition. Thereby I start with a discussion of my ontological position. In philosophy ontology (Greek for being) is the study of conceptions of reality and the nature of being. Epistemology is the study of knowledge creation of this reality. I view actors as participants in a process influenced by an evolving institutional framework. When taking an actor-institutional approach to this I try to describe organizations as complex political systems with agents organized into sub-coalitions with seemingly irrational and non-maximizing decision models. This is a view far removed from the concepts governing the rational and economic man, who is an informed, competent decision maker, always ready to make a rational utility-maximizing choice.

To further complicate my view of the human being I have made additional assumptions of man's actions as being socially constructed. Sociologist Alfred Schütz points out that it is impossible to understand human conduct while ignoring its intentions, and it is impossible to understand human intentions while ignoring the settings in which they make sense (Schütz & Luckmann, 1973; referred in Czarniawska, 2004:4). Schütz greatly influenced Berger and Luckman (1961/1991) who claim that:

> "And in so far as all human "knowledge" is developed, transmitted and maintained in social situations, the sociology of knowledge must seek to understand the processes by which this is done in such a way that a taken-for-granted "reality" congeals for the man in the street. In other words, we contend that the sociology of knowledge is concerned with the analysis of the social construction of reality." (Berger and Luckman, 1991:15)

The common features of social constructionism are a rejection of a dualistic ontology, of an objectivist epistemology, of the individual as the foundation of knowledge and of language as a mirror of objective reality. Instead, social constructivism regards subject and object as an inseparable relation. In the social construction of reality, there is an ongoing dialectical process between subjective and objective reality.

Put in an organizational context, this means that coalition partners may have distinct preferences and objectives that make negotiation and bargaining among coalition members commonplace. Shifting coalitions of organizational actors affect organizational decisions, goal setting, and problem-solving processes. This thinking is inspired by Weber (1910–1919/1983), who has influenced later thinking on how a relationship develops (is constructed) between people of different positions within an organization (i.e. bureaucracy).

Together the ideas of rational decision-making behaviour and of bounded rationality (Simons, 1957) can be used to illuminate the different tools (legal and norms) that actors (such as board members) have at their disposal (actively or passively) during a corporate control contest.

4.2 The methodological perspective

My purpose with this dissertation has been to identify the dominant forces driving a cross-border hostile takeover process in financial capitalism and to understand how takeover regulation shapes the outcome. For this I have felt it natural to pursue a number of case studies.

The legitimacy of these and other case studies rest on the assumption brought forth by Ragin and Becker (1992) that an investigation can be used to provide evidence of any social phenomena of a more general importance. Embedded in the case is the assumption that it stands for certain general features of the social world focused in a particular circumstance. Cases come wrapped in theories. The logic of the case study is to demonstrate a casual argument about how general social forces take shape and produce results in specific settings. The final description is expected to say something about the potential generality of the results. As such a particular case and what it represent offers an opportunity to develop or revise connections between both established and new explanatory concepts, often then formulated as empirically based theories ready to deliver an answer to the question *what is it a case of?* (Ragin & Becker, 1992:6). Flyvbjerg (2004) argues that qualitative methods and case study research may be used both for hypothesis testing and for generalizing beyond the particular cases studied. Multiple case studies increase the possibility of drawing more general conclusions.

In all, I conducted six studies. The first two are purely descriptive studies of the Swedish governance regime and takeover market. Three of the studies that I have done can be described as longitudinal single case studies. These evolve around a target company in a cross-border hostile takeover process. The view is taken that each case can be deconstructed, along the lines presented by Abbott (in Ragin & Becker, 1992:63). This deconstruction process starts off whole and gets simplified. Social laws are inevitable ingredient in this deconstruction, as things happen because of constellations of factors, not because of a few fundamental effects acting independently.

Academic research can be designed as either quantitative or qualitative. In social science a quantitative study is defined as a systematic empirical investigation of social phenomena via statistical, mathematical or computational techniques. A qualitative study in contrast is often characterized by rich, open and multi-meaning empirical material as well as perspective emanating from the study-subjects own perspective (Alvesson & Sköldberg, 1994; Bryman, 1989). Qualitative studies are often conducted using documents, artefacts, interviews, and observations (Silverman, 2001). Alvesson and Sköldberg (1994:27) claim that a qualitative method need not be inconsistent with an analytical perspective: "If there are hidden patterns…that govern the observed parts of reality, and if the latter can be explained by investigating the former, this would seem to be a legitimate area of research."

My chosen case study approach has also borrowed ideas from grounded theory, a qualitative empirical research model set up by Glaser and Strauss (1967). Grounded theory is an inductive type of research, based or "grounded" in the observations or data from which it was developed; it uses a variety of data sources, including quantitative data, review of records, interviews, observation and surveys. The focus is on theory generation rather than on theory verification. The data includes both inductive and deductive thinking where the researcher alternates between the material – interviews and documents in an abductive process (Alvesson & Skjöldberg, 1994) to be able to answer the research question. The perfect abductive method, developed by Charles Sanders Peirce in the late 1800s leads to a research practice where data sampling, data analysis and theory development are not seen as distinct and disjunctive, but as different steps to be repeated until one can describe and explain the phenomenon that is being researched. The stopping point is reached when new data no longer changes the emerging theory.

The three case studies target Old Mutual's hostile takeover of Skandia (2005), the fight over Scania, with a special focus on MAN's hostile bid (2006) and private equity firms' Nordic Capital and Apax joint hostile bid on Capio (2006). The concrete question I wish to answer is "*Why* did these occur?" This spurred a more accessible question to answer, which was "*How* did they occur?" With material from these three case studies it was all too thrilling to add the question "*What* did this mean?" It is from this latter what-question the fourth case study of Swedish takeover regulations was conducted with a special focus on the changes made in the 2009 revision of the Swedish takeover rules. The fourth case study, dealing with takeover regulation, is mainly a comparative literature study of legal documents. Yet these documents have been chosen for a purpose, that to construct an interpretation of the empirical material.

It is important to understand that this dissertation, neither in the theoretical chapter, nor in the empirical case studies, aims to address the issue of *who* shall own a listed company, but rather how the ultimate decision to transfer influence from one corporate owner to another is made. This means that the research, neither the theory nor the empirics, evaluates the quality or the strategy of the bidding party or the economic rationale of the ultimate owner (be it a private equity firm, an activist, a sovereign wealth fund or an industrial owner). Nor does the analysis address the effects to other constituencies ex post the (hostile) takeover, such as creditors and employees. The dissertation targets the takeover process ex-ante. Seen together as a group the six studies contributes to the understanding of how the social process of the Swedish takeover market came to work during the sixth takeover wave.

4.3 The researcher's perspective

In accordance with the long research tradition in socioeconomics, I did not begin my studies as free from some kind of *tabula rasa*. I had received an MSc from Stockholm School of Economics in the middle of the 1980s and since then spent 25 years in financial journalism covering large Swedish listed companies for different media in Stockholm.[35] I had also co-written books about two Swedish multinational companies that crashed shortly after the millennium, ABB and Skandia.[36]

During the years I wrote articles on most of the takeovers and corporate control-fights involving actors on the Stockholm Stock Exchange. Through the years I noted two things. First, the numbers of takeovers, including cross-border takeovers, increased. Second, the process governing the success of the bidding party during the takeover changed. During the sixth takeover wave conflicts between actors increased. It seemed as if the bidders, target boards and target shareholders, disagreed more often than not. The reasons varied and it was difficult for an outsider (such as a business journalist) to follow the ongoing power play. To be able to understand what was going on I turned to studying the Swedish model for corporate governance.

Working at Dagens Industri in 2005, I covered Old Mutual's bid on Skandia. That meant that in the autumn of 2006 when I was offered the opportunity to pursue a study of the deal I was already familiar with it, both the actual story and the actors involved. The Old Mutual-Skandia research can also be seen as an independent follow up of my book on the

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[35] These include Affärsvärlden, Finanstidningen, Dagens Nyheter, www.E24.se and Dagens Industri.

[36] The books deal with ABB (Carlsson & Nachemson-Ekwall, 2003) and Skandia (Nachemson-Ekwall & Carlsson, 2004).

Skandia crash, drawing on that previous supply of practical knowledge of the company and its environment.

When the Skandia research started in December of 2006 there was already a running research programme at the Stockholm School of Economics Centre for Management Studies addressing governance and control issues associated with the emerging global financial capitalism. The case study was conducted together with Professor Sven-Erik Sjöstrand and Assistant Professor Markus Kallifatides. Sjöstrand had previous experience from conducting longitudinal, multi-method studies of senior management and governance practices in many Nordic corporations. This meant that there was an extensive, well-known and trustworthy network in place, making comprehensive empirical access possible. Kallifatides was well positioned to handle the theoretical setting.

The other case studies, those of Scania, Capio and the takeover regulations I conducted on my own. Even in those cases I had prior knowledge. I had covered Scania during my journalistic career, writing extensively about all its power struggles. I had also written a few articles about Capio, and the parties involved in this contest were to a large extent well known in Sweden. I had not covered takeover regulation but reported sporadically on the European Commission's work with the takeover directive, the different codes of corporate governance in Sweden and abroad, the regulatory environment of the stock exchange and followed the work of the self-regulatory body, the Swedish Securities Council.

4.4 Six studies[37]

4.4.1 Descriptions of the institutional setting

The first two studies describe the institutional setting of Sweden and how governance and regulation have evolved to cope with financial capital-

[37] An extended description of each of the four case studies is presented in Appendix.

ism. The studies are based on a mixture of public material, books and academic reports. The first study describes the development of the Swedish corporate governance system. The second study describes the Swedish takeover market. Both studies constitute background material for the understanding of the three empirical case studies, the setting of financial capitalism and the revision of the takeover regulations in 2009 (the sixth study). The purpose of the two background studies has been to detect possible patterns of path dependency and social embeddedness on a national market for corporate control. Behind the first study of the governance system lays the assumption that the choice of governance regime has implications for a cross-border hostile-takeover process (i.e. it is a social process). The focus has been to reveal patterns that facilitate or hinder a takeover. There are plenty of descriptions of the Swedish governance model but to my knowledge there is no previous description that analyses what certain features present in the Swedish governance model might mean in relation to a cross-border hostile takeover in financial capitalism.

The second study offers a perspective on the Swedish takeover market and regulations. This study was pursued for two reasons:

- Takeover regulation, codes and company law, appeared to influence the outcome of all the three bids. Regulations appeared to influence the actions taken by parties, which appeared especially relevant in the actions taken by the board of directors of the target companies. There also seemed to be a certain amount of regulatory arbitrage, through which informed actors took advantage of regulatory differences between nations. With this in mind I felt it to be of interest to study the regulatory environment to find out how it related to the theoretical construct of an efficient market for corporate control.
- My personal interest in the legal framework of the listed company also played a role in the choice to include takeover regulation in the empirical part of the dissertation. Through the years I had covered most of the high-profile cases dealt with by

the self-regulatory body the Swedish Securities Council. I had also written extensively about the Swedish code of corporate governance.

Both background studies include a section with comparison with other countries such as Germany, the UK, and the US and in some part also the Nordic countries Norway, Finland and Denmark. The UK and Germany is of special interest as two of the bidding companies emanate from these governance regimes. The US is included for three reasons:

- A great amount of the theoretical development of a market for corporate control emanates from a US context. This includes the development of financial market theory and the idea of shareholder value as a "superior" governance model.
- Many of the actors involved – including investment banks and institutional investors, came out of an American context.
- Understanding the divergence between the UK and the US appeared important as a comparative analyses, both countries being liberal market economies. Understanding these differences helped understanding differences in governance procedures within the group of member states of the EU.

4.4.2 Case 1: Skandia

Skandia was chosen as an in-depth case since it was assumed, from the writing in media (see below), that it could work as a good example for the struggle of corporate control on a modern financial market. It was also assumed to give insights that could be applied, in part, to other deals involving Swedish companies in general and cross-border hostile takeovers in particular.

The Skandia case was presented as a narrative, published in the book: *Corporate governance in financial capitalism – Old Mutual's hostile bid on Skandia 2005* (Kallifatides, Nachemson-Ekwall & Sjöstrand, 2010). Narratives are texts that present events developed in time due to impersonal causes or human intentions. They were the main carriers of knowledge in modern societies toward the end of the 20th century (Czarniawska, 1998). This mode of presentation was chosen to match a chronological presentation of the "pure" empirics while at the same time offering a platform for both a theoretical and practical discussion.

A written narrative is sustainable for material that makes no claims to recount eternal truths. As Bruner (1986) stated, the narrative mode of knowing consists in organizing experience with the help of a scheme assuming the intentionality of human action. It is crucial to see that narrative, unlike science, leaves openness in the conclusions and thus enable competing interpretations. As such the narrative produces stories, which Bruner (1986) claims are "especially viable instruments of social negotiation". The struggle for Skandia, with agents of conflicting goals, is a good example of this (the method is further outlined in the *Appendix*).

The Skandia narrative ended with a few questions, suitable for further study, which could take this dissertation in a number of different directions. I decided to search for more target takeover candidates that had received public attention through coverage in media or engagement by the Swedish Securities Council (which in almost all cases were parallel activities). I chose to continue with cross-border hostile takeovers to learn whether similar or additional problems showed up in other bid fights during the sixth takeover wave, involving Swedish targets. In total there were 80 public takeovers in Sweden during the sixth takeover wave (2004–2008).[38] This is approximately twenty a year and equivalent to seven per cent of the listed companies. Of the bids, 45 fit the description of cross-border bids.

4.4.3 Cases 2 and 3: Capio and Scania

Compiling a list of hostile bids was more difficult. To select them I relied on the definition of a hostile bid as being a bid that has not received initial support from the target management and board of directors. This is

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[38] Sundqvist, S. *Ägarna och Makten*. Aktieservice (2004–2009).

Manne's (1965) definition of a hostile bid. However, given the Swedish context where bids are tendered straight to the shareholders, it can sometimes be difficult to determine if a negative stance from the board is related to price alone, or if there are also considerations related to a company's future potential as an independent company. Only the latter stance defines as a true hostile bid. Equal confusion is the situation where management and board perceive there to be a risk of a hostile bid, as that perception by itself might influence actions taken by the board and management. In a number of cases a bidder negotiates directly with a controlling blockholder beforehand, but once the bid is presented in public the minority shareholders turns it down. These bids can be described as ”semi-hostile”.

To identify the relevant group of hostile bids to study in more detail I used public material including statements from the target companies, media-reports and statements by the Swedish Securities Council *(Table 5).* I could sort out a group of eighteen target companies that appeared to be suitable for studying the hostile phenomena, both from an empirical and theoretical perspective.[39] The list included bids were the originating bidder was domiciled outside Sweden, which also included bids initiated from offshore constituents. When the research narrowed down to cross-border hostile bids less than a handful of candidates were left. Besides Skandia, these were Gant (bid by Swiss Maus Frères, 2007), Capio, Scania and IBS (where the activist US fund Deccan set the agenda for the company).

[39] I do not claim that the list is exhaustive. To assure completeness a study of each and every takeover case would have to be conducted. However, the list reflects of media coverage and actions taken by the Swedish Securities Council.

Table 5. Hostile bids on the SSE during the sixth takeover wave

Year 2004–08	Target	Bidder/Bidders	Country	Comment
2008	Q-Med	EQT and largest owner Ågrup	Offshore PE firm and family	Unsuccessful. Shareholders said No.
2008	Telia	France Telecom	France	Unsuccessful. Preenstested bid failed
2008	Securitas Direct	EQT	Offshore PE	Successful. Bid rise. Controlling parties sold.
2007—08	IBS	Deccan	US	Breach of MBR.
2007—08	Telelogic	IBM	US	Successful. Bid rise and stay-on package to management.
2007	GANT	Maus Frères	Switzerland	Succesful. Bid rise.
2007	Invik	Milestone	Iceland	Successful. Bidfight over bid premia on A-shares
2007	Lindex	Stockman/ also Kappahl	Finland	Successful. Bid rise and bidfight.
2007	Cision	Triton	Offshore PE	Unsuccessful. Shareholders said No.
2006—08	Scania	MAN, also involving VW and Investor.	Germany	Unsuccessful. Investor sold to VW, breach of MBR.
2006—07	Tradedoubler	AOL	US	Unsuccessful. Alecta took a corner. Bid not prolonged.
2006	OMX	Nasdaq and Borsa Dubai/ Qatar Holding	USA/Dubai	Successful. Bidfight led to bid rise. Stay-on package.
2006	Capio	Nordic Capital and Apax	Offshore PE	Successful. Bid rise and threat of delisting.
2006	Gambro	EQT and Investor	Sweden/PE	Successful. Bid rise and threat FMR
2005	Skandia	Old Mutual	UK	Successful. Threat of FMR.
2004	Song Networks	TDC/ also an Tele2	Denmark	Bid fight, bid rise and breach of due diligence. Pre buying of stocks.
2004—07	VLT	Mediaintressenter/ Stampen	Sweden	Bide rise, delisting and FMR
2006	Mekonomen	Ax:Johnson	Sweden	Breach of MBR

Ägaren & Makten (2004–8)

I also looked for companies that had a board and management that might have acted beforehand to prevent a hostile bid from being brought forth (*Table 6*).

Table 6. High profile control fights during the sixth takeover wave

Year 2004–08	Target	Bidder/Bidders	Country	Comment
2009	Cadbury (UK)	Kraft (US)	UK/US	Two foreign parties
2008	Tietoenator (Finland)	Cideron/Nordic Capital (Offshore PE)	Finland/ Sweden	Two foreign parties
2006–08	Eniro (Sweden)	Dispersed ownership/ Hermes	UK	Pressed for payouts. Resulted in a strained financial position.
2005–07	Boliden (Sweden)	Dispersed ownership/ Landsdowe	UK	Unsuccessful. Pressed for payout.
2004–07	Swedish Match (Sweden)	Dispersed ownership/ TCI, Parvus	UK	Pressed for payouts

Media reporting indicated that this might involve a small group of companies with a dispersed shareholder structure. The group included Boliden, Eniro and Swedish Match: At the time all three had foreign domiciled activist institutional investors involved in corporate governance procedures, including the election of directors. I also tried to compile a list of cross-border hostile bids conducted outside Sweden that might be relevant to study. This list only included two target companies, Finish Tietoenator (where PE fund Nordic Capital presented a bid in 2007) and British Cadbury (where US-based Kraft bid in 2009).
To finally sort target case studies I took the following steps:

- Richness of public material, from the involved companies, through media reporting and additional activities from other bodies such as the Swedish Shareholders Association, the OMX Stock

Exchange or the Swedish Securities Council. Richness was defined as material offering a broad variety of information revealing different perspectives on a deal.

- The supposition that the case could be covered sufficiently without extensive contact with involved parties. Omitting interviews with actors was connected both with time (making and compiling interviews is both time consuming and expensive) and scope (interviews allow for a broader variety of issues to be discussed, which would broaden the perspective of this dissertation rather than focus it).

- I also made an extra check of the bids "importance" by looking at media coverage in the database www.retriever.se.[40] The combination "Scania" and "MAN" generated 5741 hits (period January 1, 2006 to January 1, 2008), clearly second to the combination "Skandia" and "Old Mutual" which generated 7990 hits (1/1/2005–1/1/2007). The combination "OMX" and "Nasdaq" generated 1394 hits (1/1/2006–1/1/2008), "Gambro" and "Investor" gave 577 hits (1/1/2006–1/1/2007) and "Capio" and "Nordic Capital" generated 90 hits (1/1/2006–30/6/2008). The combination Securitas Direct and EQT generated 113 hits (1/1/2007–30/6/2008). Just to give a few examples.

The final selection of Capio as a case study was made in June 2010. Capio was chosen as the media coverage indicated that it might reveal patterns similar to the Skandia study. This included a dispersed shareholder structure, the involvement of the same group of institutional investors that also acted in Skandia, the presence of investment banks (many also known from the Skandia case), media reports on conflicting views between directors and management representatives and the application of the forced-merger rule to press through the bid in the end.

[40] The database replaced www.affarsdata.se in December 2012. The coverage of Swedish business press can be assumed to be the same.

The Scania study commenced in September of 2010. Scania was selected to broaden the perspective. First, the Scania fight started of with a controlled ownership structure embedded in the Swedish corporate governance model with multiple voting rights in the form of A and B shares. Second, the hostile bid came from bidders in Germany, a different governance regime than Old Mutual's British background. Third, the legal dilemma of the Scania case differed from that in Skandia. In addition of course, the media coverage indicated that the available conflicts might allow an interesting story to unfold.

The starting point for both studies were the same. First I made a selection of as much public material I could find using open sources such as newspapers, weekly's and public corporate information. I then read through the materials with the aim of reconstructing the events. In this phase I both plotted a timeline of the events and tried to sort out the group of actors that appeared to be important for the process to move forward. Parallel to this work, I searched for patterns in the material that could be used to either validate findings from the Skandia study or broaden the knowledge base.

The method used to select among the public material followed the same pattern in both cases. The method was journalistic in the sense that the aim was to gather "as much information" as possible to be able reconstruct what happened as accurately as possible. I started off by reading articles relevant to the particular activity, the hostile bid. In each text I acted like a detective, looking for traces of evidence to use as reference points when continuing my research in different directions. This was all done using the data base www.affarsdata.se (and later www.retreiver.se). However, as in any single case study the method had to be adapted to the individual object. As a result the actual work with material from Capio and Scania differed (see more in appendix A).

4.4.4 Revision 2009 of the Swedish takeover regulations

The fourth case study revolved around the Swedish takeover regulations, especially the 2003 version of the NBK takeover rules and the amendments to the 2009 revision of the takeover rules. The study was not evident from the start of this project, but rather something that emerged as the dissertation work progressed. One obvious reason for this was that the Skandia case started to unfold in December 2006 and my doctorate studies commenced in December 2007. The seventh version of the NBK takeover rules did not come into force until the spring of 2009. A minor revision was done with amendments to the Swedish Takeover Rules in 2012 (i.e. the *eight revision*).

The analysis of the takeover regulation in relation to cross-border hostile takeovers during financial capitalism was done as a way to increase the understanding of the cross-border dilemma. To my knowledge, there do not exist any studies that include a comparative analysis of multiple cases in relation to developing takeover regulations. Previous studies have mainly been conducted either by legal academics, within the field of law, or financial economics, focusing on quantitative research. Pursuing a multiple qualitative analysis within management and organisation could thus be presumed to convey new and unpredicted results. I basically spent my time trying first of all to understand the regulations, asking the question *why* the regulations have emerged? This issue was targeted in the two background studies. Subsequently, I tried to sort out the way in which the regulations influenced the outcome of the bids, especially using the perspective of the activities carried out by the directors of the target company. This task was accomplished by asking the question *how* the regulations have influenced the actions taken? Finally, I have related my modus operandi to the theoretical idea of an efficient market for corporate control. This left me with the last question: *what* do these regulations imply? In the abduction of the material related to the amendments to the 2009 Takeover rules I looked for traces with the purpose of supplying answers to the following questions:

- Why were the takeover rules rewritten in 2009?
- Which problems were addressed and which were not?
- What can possibly explain the selection of issues to address or not address?

In order to answer the first question I relied on public material and interviews. The second question was answered through studying the material in the three case studies, comparisons of different regulations and academic papers.

This sixth and final case study includes rich comparisons to the EU Directive on Takeovers and to the British, German and US takeover regulations (for a more detailed description of the method see *Appendix*). As an analytical exercise I also included the hypothetical question, what would the outcome have been if the takeover rules revised 2009 had already been in place during the bid-fights accounted for in the three case studies? Would the enforcement of these rules have changed the outcome? Of course, this is something that neither I nor anyone else can know anything about. However, as an analytical tool it has some merit.

4.7 Methodological endnote

The work with this dissertation was not conducted in a vacuum. During the period I was offered plenty of opportunities to refine my theoretical and practical understanding of corporate governance and financial capitalism. This included the production of a number of reports, all published in Swedish. These include a report on the development of the Swedish ownership market for SNS (August, 2008), *Centre for Business and Policy Studies*; A chapter: "EU and corporate governance, after the economic crisis" (2010) for SNEE *Network for European Studies in Economics and Business*. I also wrote the report "Institutional investors' ability to pursue responsible owner governance in listed companies" (January, 2012), for the *Confederation of Swedish Industry* (*Sw:* Svenskt Näringsliv). I co-authored two conference papers (Kallifatides & Nachemson-Ekwall, 2010, 2012).

Chapter 5

A Swedish perspective on governance

5.1 Purpose and structure of this chapter

Previous chapters have described the theoretical platform of an *efficient market for corporate control* open for cross-border hostile takeovers, how it has evolved and how this can be understood in an institutional theoretical context. This has been done through the lenses of finance, law and management. Seen as an integrated toolbox for a cross-border hostile takeover process, this eclectic research methodology establishes a theoretical framework built on an institutionalist perspective. This chapter and the one following, Ch. 6, can be read as background material to the four case studies of this dissertation. In this chapter I describe the institutional setting for the Swedish market for corporate control in relation to the Swedish model of corporate governance, often described as "governance by owners" (e.g. Carlsson, 2007). In the next chapter I describe the development of the Swedish takeover and ownership market in more detail, including the role of institutional investors and the forming of the Swedish takeover regulations. Both chapters relate Swedish governance and takeover regulation to the UK, US and Germany.

To begin with, a general description of how the Swedish market has evolved and how academics, largely from finance and economics, interpret this development, is presented. Since my belief is that this presentation seems to single handed portray the owner-governance as being a "best-model", the perspective is broadened to enable a more open analysis of the specific Swedish governance model in the context of path dependency and social embeddedness. This open perspective explains how the Swedish model has developed along two parallel tracks, one formal (legal) and one informal (societal). To enhance understanding of what this development might entail the Swedish owner-governance model is compared to the British, US and German governance models. The former two offer two variations of shareholder models whereas the latter offers a perspective of the stakeholder model. The chapter ends in an understanding of why convergence of national models of governance has not happened as expected, national governance systems being dependent on past experience, corporate law as well as culture and social embeddedness. The actual development of the Swedish takeover market and how the three theoretical drivers presented in Ch. 3 have been put to use on the Swedish market is presented in the next chapter.

5.2 Takeovers embedded in a Swedish governance model

As background, the Swedish stock market has for some time featured an active market for corporate control, including a number of takeovers since the 1990s. The Swedish market for corporate control has been second only to the UK. During the fifteen year period 1990–2004 a total of 358 takeovers took place the great majority of which, 331, were addressed to shareholders and 293 closed with success (SOU, 2005:58).

Swedish academic studies have pointed toward specific national governance mechanisms that have influenced the merger and acquisition trend, such as differential voting rights and blockholder structure, that seem to have facilitated sell-outs (Angblad, Berglöf, Högfeldt & Svancar, 2001; Tson Söderström, 2003; Högfeldt, 2003). The large presence of voting differences can simplify the bidder's negotiation with target shareholders who control blocks of shares while reducing the attractiveness for the remaining minority shareholders to remain owners (Burkart, 2005). The structure of the Swedish tax system also seems to have disfavoured private wealth creation, thus, reducing the formation of domestic capital that is readily available to invest in (Swedish) companies (Henrekson & Jakobsson, 2005). This has included a progressive personal income tax and the taxation of dividends from the firms, taxed both through corporate tax and capital gains tax at the household level.[41] The latter does not target institutional investors and foreign citizens. To this can be added the collectivisation of domestic savings that seem to have distorted the role and power of the traditional Swedish ownership and control model (Henrekson & Jakobsson, 2005). Thus, Sweden belongs to a large family of countries where control by blocks of shareholdings is the dominant corporate governance model. Unique to the Swedish model, though, is that the wealth on which the controlling ownership is based had become extremely thin by the 1990s, probably thinner than in any other country (Angblad et al. 2001). Therefore, among the countries characterized by blockholder control of listed firms, the Swedish control model could be expected to be more vulnerable both to the forces of globalization and the growth of institutional ownership (Henrekson & Jakobsson, 2005).

To fully understand the implications of the Swedish governance model I claim it to be relevant to describe specific features of the Swedish governance model and how these have come to work in financial capitalism. First, the previous focus on taxation is here complemented with a description of Swedish company law, and how it relates to governance issues. Secondly, blockholder governance is complemented by a description of informal governance in a society moving from governance built on stakeholder values to governance built on shareholder values. The chapter ends up with a discussion of what this

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[41] Sweden has since 2000 lowered personal income taxes, corporate taxes and abandoned wealth tax and inheritance tax. However, the tax on dividend and profits on stock transactions have remained more or less unchanged.

transformation might imply for the Swedish model of “governance by owners” in financial capitalism.

5.3 The Swedish legal governance model

As an historical background the Swedish corporate governance model was formed during the early 1900s, a period of committed industrial ownership and a focus on value creation. Two men were particularly important for the development of corporate governance procedures during this period: Marcus Wallenberg Sr., ”the Judge” (1864–1943), and Ivar Kreuger (1880–1932). Marcus Wallenberg, as a large shareholder, sought to control the management activities of a number of listed companies. To be able to do this he fully separated the board from management, a governance structure featuring three independent legal organs (see *Figure 7* below) that still is viewed as a major reason of the successful value creation in Swedish industry (Carlsson, 2007).

Ivar Kreuger, with his international conglomerate Swedish Match, introduced differentiated voting rights in 1910 when he looked to London to raise money to his listed companies. Currency and ownership regulations prevented foreign investors from exercising influence on Swedish companies, so stocks with differentiated voting rights were introduced, with the share series offering the stronger voting rights kept for Swedish investors. With these two men in mind, two features of Swedish corporate governance have become especially prominent:

- A clear distribution of responsibilities between shareholders at the Annual General Meeting, the board of directors and the executive management. Except for the CEO, which is sometimes a board member, all directors are non-executive, including the chairman. There is also a clear separation of responsibilities between the chairman and the CEO. This was included in the 1946 version of the Swedish Companies Act.

- A system of dual shares/differentiated voting rights. Today it comes in the form of A shares with one vote and B shares with a tenth of a vote. Systems of different voting rights exist in other countries too, i.e. in the US. But in no other country is the usage as common as in Sweden. The mechanism with differentiated voting rights became widespread during the Social Democratic regime.[42] 18 per cent of all listed firms used dual - class shares in 1950; by 1981, that number had increased to 54 per cent. In 1992 the percentage of listed firms offering dual-class shares topped at 87 per cent.[43]

Against this historical background Sweden has developed specific features in its corporate governance model in relation to board representation. The Swedish model of corporate governance, which show similarities with the Nordic countries of Finland and Norway,[44] allow proxies to be controlled by the shareholders, and not by the board as in the case of the US. Thus it is the shareholders that both suggest and vote for the appointment of directors on the board. These are then elected for a one-year mandate. In principle there is a separation of power between the board of directors and the management, as shown in *Figure 7*, with the CEO solely responsible for day-to-day matters. The CEO might be a member of the board, but this is not always the case, and the trend is clearly for the exclusion of the CEO.[45] Thus, in the Swedish governance model, all directors have been (formally) independent of the corporation to begin with.

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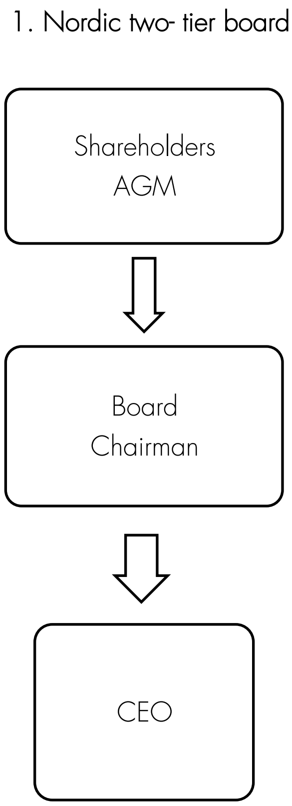
[42] Sweden experienced a more or less stable period of left-of-centre government from 1932-1976.

[43] After that the usage fell back to close to 40 per cent by 2010 (Henrekson & Jakobsson, 2012), reflecting both pressure from an investor community dominated by international institutional actors and a large number of smaller IPOs.

[44] For detailed information The Swedish Corporate Governance Board.

[45] According to Fristedt and Sundqvist (2010) the CEO is not a member of the board in 55 per cent of the boards. The Swedish Academy of Boards of Directors recommends excluding CEO from board representation.

Figure 7. The Nordic governance model



Swedish Corporate Governance Board (2012)

Large shareholders are expected to be on the board and even to be the chairman. Up till the middle of the 1990s it happened occasionally that a CEO retired as chairman, but this is now seldom the case and the Swedish code of corporate governance recommends against it. It is stated in the Companies Act (8 Ch. 4 §) that while serving on the board, all directors have to act for the sole interest of all shareholders alike. Neither the board nor any of the company's legal representatives may carry out activities that are geared at favouring a specific shareholder in relation to the other shareholders or the company. The board is required to act as an agent for the whole shareholder group in a hypothetical sense, ("the principle of equality" or *Sw.* "gestor"; Svernlöv, 2007, p. 309; Nerep & Samuelsson, 2009). Applied to Swedish capital markets law the director's fiduciary obligation is extended to include also responsibility to act also for previous and future shareholders (Stattin, 2009, p. 64), in a hypothetical sense equating the interest of short-term traders and long-term blockholders.

The governance balance between the blockholder and other shareholder groups is open for interpretation, as owners in control of more than 50 per cent of the votes in the company (during the AGM) can enrol all directors and thus dominate the work of the board. The Swedish code of corporate governance, built on the UK comply-or-explain model, states that two directors should be "independent" from the largest shareholder. However, it is left to the company to deliver the explanation as to what is considered to be an independent director, which has the effect of giving a certain freedom in the enrolment of directors. Similarly, as the code does not prevent the largest shareholder (during the AGM) from voting against directors, the "independent" directors still rely on the support of the majority shareholder.[46] Thus, protection of minority shareholders is a very important feature in the Companies Act.

A shareholder value focus does not mean that the interests of employees are not taken into account. Employee participation on company boards was introduced in Sweden in 1973 by way of legislation (for a description e.g. Victorin, 2000). Current legislation was enacted in 1988 and is a consolidation of the 1973 act with certain amendments. The Swedish and German systems of co-determination work very differently (see section 5.4). In Sweden, the local branches of the trade unions representing the employees have a collective agreement relationship with the employer. Wages and strikes are generally handled without involving the board of directors. In companies with more than 30 employees, the local unions have a right to appoint two board members. If the number of

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[46] The Stockholm Stock exchange listing requirements of 2003 includes the presence of two independent directors. In 2010 this was taken over by the Code instead as a recommendation of 'best practise', thus allowing more flexibility for the companies.

employees is 1000 or more, the number of board members is increased to three. In general the employer, as represented by the shareholder elected directors, is concerned with giving the union representatives information on company matters. At the same time the employee directors are not very active in the boards general work. They do not interfere with strategic issues, but tend to be interested in personnel matters and other issues that concern the employees more directly, such as the work environment or re-organizations.

Since the middle of 1990s Swedish governance has also seen the emergence of a third distinct feature of governance – *nomination committees* – as a forum for large shareholders to discuss members of the board of directors to be suggested at the next Annual General Meeting. The rationale behind the nomination committee can be seen in the context of A and B shares where institutional investors, often only owners of B-shares but large contributors of equity capital, wish to have a say in the recruitment of new directors ahead of the AGM.[47] The nomination committee was formalized in the first Swedish corporate governance code 2006, which recommends that the names of members of the nomination committee is announced no later than six month before the AGM, which will usually be shortly after the Q3 report. The chairman of the board is supposed to be a member of the committee, but not to chair it. The established process has become to register nominees from the four largest shareholders six month before the AGM. However, some companies announce the composition of the nomination committee at the AGM the previous year, which is the recommended procedure from the Swedish Shareholders' Association.

[47] The first test of a nomination committee was to be in the search of a new director in Volvo, which lacked a dominant shareholder, after the shareholder revolt over the Renault/Volvo deal in 1993. At the time, it was an all-Swedish matter.

5.4 The Swedish informal governance model

The legal development of the Swedish governance-model is here complemented with a description of how informal governance came to develop in Sweden in the post-war period up to the deregulation of the Swedish capital market around 1990.[48] Swedish ownership around the 1950s resembled very much the corporate structure of the periods between the first and second World Wars. The larger Swedish companies were already formed and the capital was controlled by a few rich families. At the same time it was the CEO that had the actual power together with the different bank spheres (see for example Östman, 2008, on the implication for the governance of financial resources). There were two reasons for this:

1. After the financial crisis of the 1920s the banks and their wholly owned investment companies [49] had emerged as controlling owners of many industries. These banks worked closer with management than with the other shareholders.
2. With the crash of the Kreuger-Group in 1933 the investment companies were separated from the banks by law. The close relationship between the banks and management would however remain well into the 1960s.

In the background a group of rich families developed their businesses, especially the Wallenbergs with the Wallenberg foundation and their own bank sphere, Skandinaviska Enskilda Banken. Most important was the previously mentioned Marcus Wallenberg. The Wallenbergs and

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[48] This description is based on Nachemson-Ekwall (2008) and Högfeldt (2004).

[49] Closed investment funds or business groups dominated the Swedish Stock Exchange up till the millennium.

their investment company Investor[50] controlled behind Swedish flagship companies such as the pharmaceutical firm Astra, engineering companies Atlas Copco and Asea, heavy-vehicle conglomerate Scania-Vabis as well as parts of the Swedish pulp and paper industry. There was also Handelsbanken, the other private banking sphere with its investment company Industrivärden, also in control of a part of the forest-industry and interests in companies such as vehicle conglomerate Volvo. Some companies were co-owned by the two spheres, such as the telecom company Ericsson.

By the 1950s four groups of "corporate elites" had control of the Swedish corporate sector; the banks, investment companies, management and the families. This order was not going to last. During the 1940s and 1950s the Swedish economy and politics changed dramatically. As indicated previously, Social Democratic policies were implemented, including a change of the tax system that disfavoured private wealth creation while at the same time supported capital formation within the established corporate sector. The tax system had by the 1960s drained most of the old Swedish families of wealth. Many of them sold their companies to the investment companies. High capital-tax and currency regulation had also left the stock market idle and unattractive for raising equity, forcing most companies to rely on bank financing instead. Since it is the management that has the contact with the banks, the real power of the corporate sector was effectively moved from the board of directors to the management. The same was true for most of the companies controlled by the investment companies. Different devices were used to protect the company from unwelcomed investors. This was especially pronounced in the financial sector where there were limits on voting power. In the insurance company Skandia, no shareholder was allowed to vote for more than 20 shares, which effectively transferred power to management. Vehicle and motor conglomerate Volvo and property and construction company Skanska developed cross holdings to protect them from outside control contest. Many others relied on pyramiding, which

[50] There was actually a group of Wallenberg controlled investment companies - Export Invest, Providentia and Investor - that in the 1990s merged to form Investor.

was especially profound in the Wallenberg and Handelsbanken spheres (Högfeldt, 2004). Recruitment of directors followed the same track – in companies with a controlling family directors were chosen among the friends of the largest owner. In other companies, were owners were absent, directors were recruited out of the network of the CEO or, in the case of bank domination, from the network of the bank sphere.

In the early 1980s Sweden joined the international trend of reforms and market liberalisation. The credit market was deregulated. Sweden opened up for foreign direct investments. The stock market exploded. Currency regulation was abandoned in 1992. A new group of wealthy Swedes was formed – with fortunes made in the financial sector and on property. Nevertheless, the Swedish informal model of governance seemed to survive.

A number of Swedish academics have tried to explain the survival of the Swedish corporate governance model as it still existed around the millennium. Collin (1998) develops an analytical framework to explain why the organizational structure of investment companies, seen as business groups, or BGs, survived as entities on the Stockholm stock market, at odds with both modern financial agency theory and the globalization of capital markets. Collin (1998) presents a typology of hypothesis based on different organizational perspectives. He finds that there is cultural support for the survival of the business groups as they have been around for a long time, that they appear to support the Swedish governance model and that they have been fairly successful at value creation. Collin also points to their success in handling of credit (through the house-banking system), governmental support for labour creation and management of a market for managerial labour as factors that stimulate the existence of BGs in Sweden. These ideas fit well with later research by Fligstein (2001) and Roe (2003), highlighting the delicate balancing act of societal acceptance that the Swedish investment companies have to address.

The reasoning above is expanded further in Högfeldt (2004), which tries to explain how the system of control and governance of the Swedish corporate sector, including the reliance of the Wallenberg's to set the general agenda, was all supported by the Social Democratic government.

Högfeldt (2004) writes that a public inquiry in 1986 about voting rights explicitly stated that dual-class shares could be useful to ascertain that "Swedish firms remain controlled by Swedish interests" (e.g. Swedish Government Official Reports, SOU, 1986:23). Högfeldt writes:

> "The political support for extensive use of dual-class shares and pyramiding is traded off against the indirect (direct) promise that the largest firms continue to invest in Sweden and do not migrate. Dual-class shares and pyramiding are in fact the very cornerstones of the Social Democratic model of corporate ownership." (Högfeldt, 2004, p. 565)

An example of this is the fight by the Swedish government at the turn of the millennium to stop the Commission's plan to abolish the right by shareholders with multiple voting-rights to negotiate a price-premia during a bid situation. The Social Democratic government at the time declared the dual-class system to be a national interest. The relevant point here is that the Wallenbergs, via Investor, was active at the same time.[51]

Quantitative regulations of asset allocation by Swedish retail funds and the national pension funds have also been applied to support a governance model built on private block holdings. Part of this can be related to an historical worry that large corporative Swedish pension funds might "socialize" the business sector.[52] There has also been a parallel worry that retail funds controlled by the four large retail banks will act in the interest of their "owner spheres" rather than act in the interest of wealth maximizing for their fiduciaries (for a description see Kallifatides & Nachemson-Ekwall, 2012).

According to the *Swedish National Pension Funds Act* (*Sw:* "Lagen om

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[51] Notably the argumentation from the Wallenberg's and the government differed at the time as the Wallenbergs (and the Confederation of Swedish Industry) would use property rights arguments grounded in both human rights theory and Alchian and Demsetz (1972) to refine their position.

[52] This worry still prevails and can be related back to the highly ideological debate of the planned introduction of the Swedish wage-earners funds in early 1980s. An account is offered in Nycander (2008).

Allmänna Pensionsfonder", 2000) the funds assets must only be "managed in such a manner so as to achieve the greatest possible return on the income-based retirement pension insurance" (Act 4 Ch. 1 §). This shall be done within risk limits and with no consideration taken to national, regional or employment interest. Each of the four funds may only own two percent of the capital in a specific company and voting power may not exceed ten per cent (Act 4 Ch. 6 §). The Investment Funds' Act (*Sw:* "Lagen om investeringsfonder", 2004) states that investment funds are not allowed to allocate more than five per cent of total assets to a single company (Act 5 Ch. 5 §). There are also limits on the level of control and influence in a single company. An asset manager with different fund products must not own more than ten per cent of the stocks in a given company (Act 5 Ch. 5 § 19:2). Voting power is addressed separately:

> "An asset manager may not to a fund buy stocks with related voting power enough to enable the asset manager to exercise significant influence over the management of the corporation." (SFS; 2004:46, Ch. 5:20)

The overall effect of the restrictions have been limited as most of the funds have had an investment strategy modelled on portfolio theory (see Ch. 2.4 and Ch. 3.4) and thus held a large number of different stocks in the funds, but it has had implications in specific cases such as takeovers (Kallifatides & Nachemson-Ekwall, 2012).

Sinani, Stafsudd, Thomsen, Edling and Randoy (2008) have mapped enrolment of directors to listed companies in the Nordic countries of Denmark, Norway and Sweden. Building on corporate networks as a possible informal governance mechanism the authors argue that all three countries can be characterized as, what they call "small worlds" in which trust, information diffusion and reputation are active governance mechanisms. Especially in Sweden and Denmark there exist clusters of highly connected directors. The research also extends the previous focus on formal institutions, such as the effect of legal systems present in the LLSV stream of literature. The result is interesting, as Sinani et al. (2008) first describe the differences that exist between the countries, both as regard to corporate structure and regulatory inconsistencies within the governance framework of the countries. But the paper also highlights that there are few cases of owners expropriating from minority shareholders in the countries, this implying that non-financial compensation in terms of reputation and status may be enough, and there are also few cases of hostile takeovers. Sinani et al. (2008) turn to *trust* to explain recruitment of directors. This is done with reference to Granovetter (2005) that emphasizes that social networks affect the economic outcomes because, among other reasons, networks affect the flow of information and trust. Collin (1998) and Coffee (2001) argue that trust can replace formal law as a governance mechanism to protect minority investors in the Scandinavian countries, which are small tight network societies. At the same time Dyck and Zingales (2002) suggest that media exposure may be an important governance mechanism, as bad performance may damage the reputation of managers and board members. This media exposure mechanism can be said to have been working in Sweden in relating to public outcry over executive pay.[53]

Today, Swedish governance works differently. The societal-trust relationship between the unions, owners/board and the government that was present in industrial capitalism (i.e. the period up til the 1970s), has in financial capitalism been replaced by governance of the capital market where owners, directors and management are concentrated on the creation of shareholder value. Currency regulation has been abandoned in favour of free capital movement and enhancement of liquid stock markets. The state and the unions have withdrawn from direct influence in a number of steps leaving a vacuum. At the same time, the owners also changed. With the old "control owners" lacking adequate wealth to finance expansion of firms (e.g. Henrekson and Jakobsson, 2005), over time also putting strain on their governance capacity, other actors with financial resources have filled that gap. In financial capitalism, both foreign and Swedish institutional investors have come to play significant

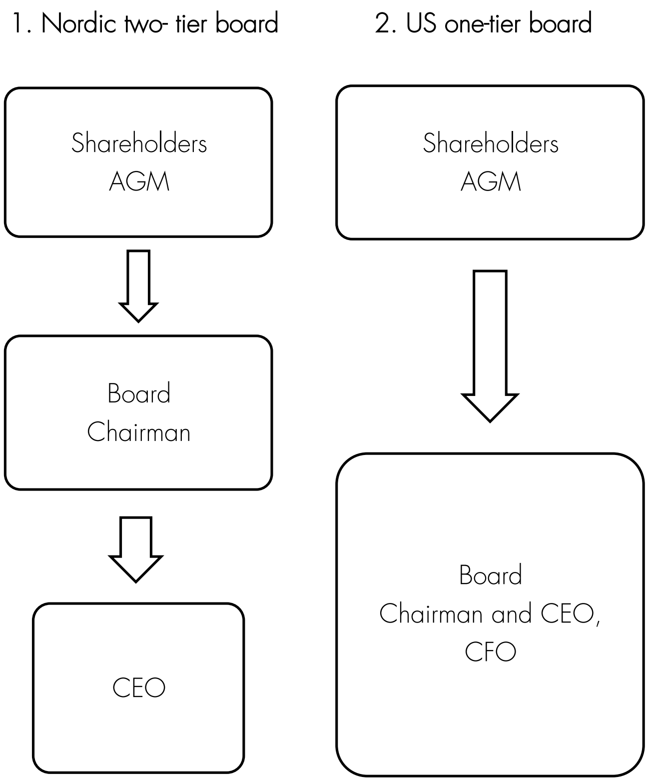
[53] There are a number of examples, of which the pension-package offered Percy Barnevik in ABB, revealed in 2001, is one of the most publicized, in Carlsson and Nachemson-Ekwall (2002). The story of the hefty payouts to the top-management in Skandia is recounted in Carlsson and Nachemson-Ekwall (2003).

roles in the development of contemporary corporate governance in Sweden. Relating to Östman (1993, 2008) this can be described as a corporate governance that has moved in the direction of the financial flow where the external forces has strengthened so much that the power balance between the operational and financial rationalities has tilted in favour of the latter. In financial capitalism the shareholder value model of governance has moved down the value-chain, also influencing the governance of individual divisions (Östman, 2008). One example is the growth of executive compensation to Swedish top executives in the 1990s and 2000s, which has destabilised the cultural societal fit in Sweden, known for its egalitarian structure and social cohesion. Thus, the collective focus on value creation of previous times appears to have been replaced by short-term quarterly based capitalism.

5.5 Relating to Anglo-American shareholders models

The Swedish shareholder model of corporate governance differs from an Anglo-American context. At the same time there are notable differences between British and American governance. The Swedish enrolment of directors differs notably from the Anglo-American context. In the latter case, the separation between the board and the management is not as clear as in Sweden, as shown in *Figure 8*. In both the US and the UK the board of directors is made up of a mixture of managers and shareholder representatives. In both countries the influence of other stakeholder groups is minimal. Also, in both countries it is difficult for shareholders to elect directors to the board. In both countries it has been common to elect directors for tenures covering multiple years. In the US the board was historically made up of an equal number of insider and outside directors. The insiders were executives, the CEO and chairman being the same person, and the outsiders suggested by the board, which often meant chosen among the CEO/chairman's friends. In the UK, the board of directors include two or three members of management, usually the CEO and the CFO and often someone else. The tradition with the CEO also being chairman ended in the UK in the early 1990s, and in the US following the introduction of SOX 2002.[54] In both cases this was in response to scandals at the time. At the same time the role of the chairman differs from its Swedish (and Nordic) equivalent.

Figure 8. Two governance-models



Swedish Corporate Governance Board

[54] The Sarbanes Oxley Act that was introduced in the aftermath of a number of corporate scandals, including the Enron crash 2001.

In the UK, the chairman takes the role of a traditional chairman, which means taking a clear role as communicator and bundler of differing opinions.

Responding to pressure from market actors during the 1990s and forward, all three systems – the Swedish, the UK and the US have independent directors on the board. But they are defined in different ways. In the UK system, half of the board of directors must be independent, in the sense of independent of both the company and major shareholders. The Swedish Code of Corporate Governance recommends including at least two directors who are independent of the large shareholders. Sweden does not have executive (insider) directors other than the CEO, and as stated previously, it is not always the case that he/she is a director. In the UK large shareholders are seldom serving as directors or involved in the enrolment of directors, as large shareholders are seen as representing a stakeholder.

In Sweden the position of the independent director can be more elusive (as stated previously). In a company with a dominant shareholder, in the sense that one shareholder or shareholder group has a majority control of the AGM, an independent director can only be elected if he or she receives support from the dominant shareholder.

In the US large shareholders can sit on the board, but seldom do because there often does not exist a controlling shareholder. In both the US and the UK it is the board that nominates new board members. In the UK the chairman also chairs the nomination committee and since the 1990s the committee is supposed to be constituted of independent directors on the board (Higgs, 2003). The suggestions are then presented to the AGM to vote on. UK directors are often elected on terms of varying length. In the UK, the Code stipulates a first term two-year mandate and a retirement for independent directors after nine years. In the US the board uses overlapping tenures - staggering boards – and directors are often voted in for three-year terms. In both the US and the UK it is rather difficult for shareholders to suggest directors. However, British shareholders do have the right to nominate candidates, but they seldom do. In the US it is more or less an impossible procedure, as the board of directors not only nominate directors but also control the proxy voting.[55] The difference between the UK and the US can partly be explained by the strength of institutional investors, such as pension funds, in the former country and the strength of the business community in the latter country. However, this does not mean that US directors are protected from accountability to shareholders. Just like British and Swedish directors, they have a fiduciary obligation to act in the interest of the corporation. In addition, US directors are subject to the *Business Judgement Rule* that makes it possible to test legally if directors have gathered enough information to be able to make knowledgeable decisions (Kirchner & Painter, 2000).

5.6 The German stakeholder model

From a Swedish perspective, the German stakeholder model of corporate governance is often dismissed as an eligible model for value creation in the interest of shareholders.[56] However, it is fair to claim that the change in Germany following the era of financial capitalism has been just as profound as in Sweden, albeit with, in many ways, different outcomes.

Until the middle of the 1990s, German companies were still controlled by other German companies through a system of crossholdings, sometimes referred to as the *Deutschland AG-system*. In this system German banks both provided debt financing and had invested in equity and held board representation as joint representatives of both debt holders and

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[55] *The Frank Dodd Act* introduced in 2010 allows shareholder groups in control of at least five per cent for two years to nominate a director, to be included in the proxy statement sent out by the corporate board ahead of the Annual General Meeting. The original idea was much more aggressive, but business groups such as *the U.S. Chamber of Commerce* opposed proxy access, fearing that special interest groups that lack business acumen or long-term vision for running a company could take over the boards.

[56] This became clear when media reported on the often heated discussions during MAN's hostile bid on Scania in 2006; also reporting in Financial Times and in the works of the Takeover Directive.

shareholders. These banks also often acted as proxies for small shareholders. As an effect the Deutschland AG system had efficiently insulated corporate Germany from international capitalism since the Second World War.

According to German corporate law, pursuing profits for shareholders is not considered to be the overriding concern and legal and normative traditions emphasise the social role of corporate activity. The German Constitution, Ch.14 (2), establishes the principle that "Property imposes duties. Its use should also serve the public weal."[57]

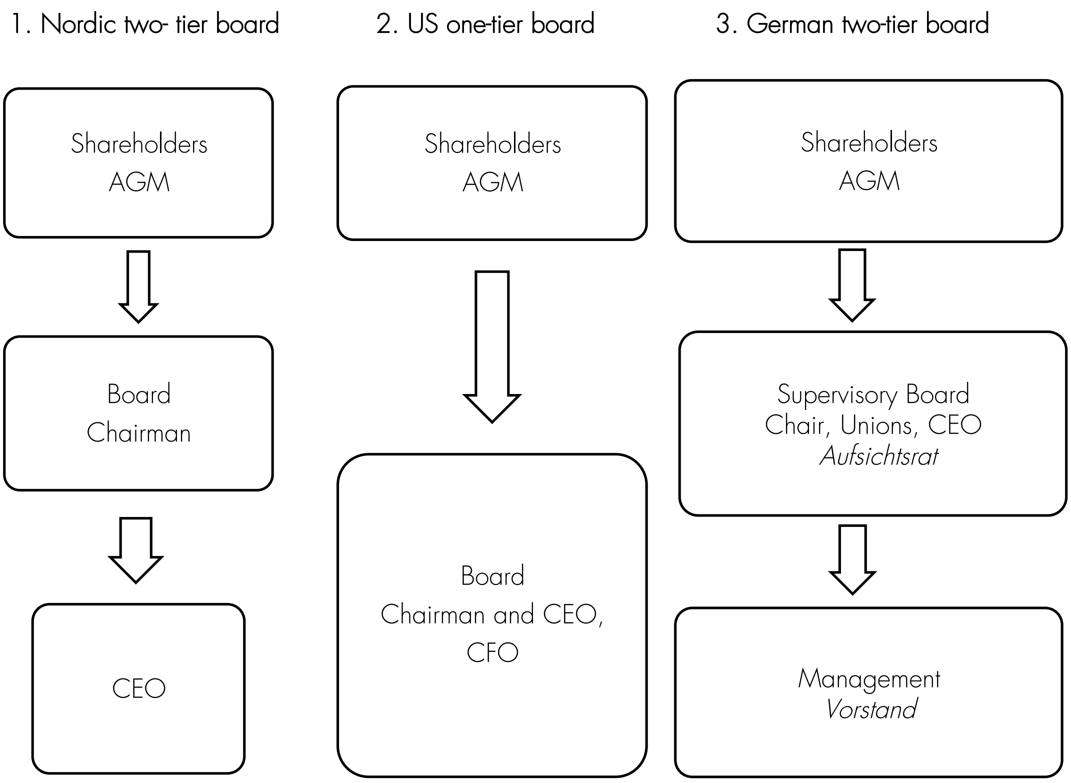
German Company law (*Gr:* "Aktiengesellschaft") has along this line developed a special model for corporate governance.[58] As shown in *Figure 9*, German governance is built around a two-tier board system that differs from the Nordic model. German supervisory boards (*Gr:* "Aufsichtsrat") are normally made up of 20 non-executive directors, with a mandate to oversee a management board (*Gr*: "Vorstand"). At the same time the German system of co-determination (*Gr:* "Mitbestimmung") ensured that the workers' unions occupied half the seats of the supervisory board, thus working differently from the Swedish counterpart. The powers of the shareholders' meeting and of the supervisory board are also restricted compared to other jurisdictions. The directors on the supervisory board are elected on a five-years tenure and can only be removed with 75 per cent of shares casted against re-election, although it is recommended in the German Corporate Governance Code that tenure should be shorter. Also, the supervisory board is not involved in the day-to-day management of the company, and as a result the German CEO and management enjoy more independence than management teams elsewhere. On paper the system more effectively delineate responsibilities

[57] The idea that there exist limits to property rights in the public interest emanate from the French philosopher Auguste Comte (1798-1857) and appears in a number of national constitutions, such as the Italian, Spanish and the German. German Constitution 14.2 says: *Gr:* "Eigentum verpflichtet. Sein Gebrauch soll Zugliech den Wohle der Allgemeinheit dienen", in van Banning (2001).

[58] Hopt and Leyens (2004) offer a number of accounts of the development of German corporate governance; also in Fligstein (2002).

than the unitary board of the Anglo-Saxon model. Historically the German two-tier model was an object of envy across the world because of the stability and long-term perspective it brought to companies.

Figure 9. Three governance-models



Swedish Corporate Governance Board

However, with the globalization of financial markets during the 1990s the Deutschland-AG system began to unravel. The system had come under scrutiny as it often led to a cosy relationship with managers and unions accepting controversial ideas in exchange for guarantees on jobs and conditions for staff. This seemed to hamper the restructuring of German industry and the growth prospects of the European economy. The German two-tier system also came under fire. The composition of the German supervisory board was considered opaque, large and out of control of shareholders. Also, a general problem with the German supervisory board was that shareholders lacked influence over management as workers could block almost every decision.

Foreign investors in particular complained. Foreign capital had increased its presence after West and East Germany were unified in 1989. The demand for capital to acquire state-owned assets then suddenly outstripped domestic investors' ability to supply it. The process accelerated as firms like Deutsche Bank, Daimler and Siemens grew through acquisitions in the US, inheriting foreign investors and taking on overseas listings. The development was echoed by the rapidly growing influence of foreign investors in other parts of corporate Germany – from bank lending to the trading of bad debts.

During the years to come the whole corporate sector embarked on a transformation, slowly abandoning the system of cross-holdings, adopting a more Anglo-Saxon system of shareholder-oriented corporate governance, with its preference for transparency and appeal to foreign investors. After 2000 the Deutschland-AG system unravelled quickly.[59] German chief executives had to find out what their diverse shareholder base thought, justifying their strategies and modifying their approach to corporate governance. Several companies turned to the European Company (Societas Europaea or SE) set up that would allow them to shrink their supervisory board to 12 members and invite foreign workers on the labour side. The smaller SE-board was expected to make discussions more efficient and the presence of foreign workers weakened codetermination, although half the board would remain labour representatives.

In modern German corporate governance the German dual board system and the single board system are converging because of the intensive interaction of the Management Board and the Supervisory Board. Still, differences remain, especially when compared to Swedish corporate

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[59] Jenkins & Milne (March 21 2005, Financial Times) present a pedagogical account of the German ownership structure.

governance. The Supervisory Board appoints and dismisses the members of the Management Board. The Supervisory Board forms a nomination committee composed exclusively of shareholder representatives that proposes suitable candidates to the Supervisory Board for recommendation to the General Meeting that are then elected on overlapping tenures. However, the union representatives on the board and the independent directors, suggested by the AGM, are equally responsible to act in the best interest of the corporation.

5.7 Conclusion

In this chapter institutional theory has been used to describe an evolving Swedish corporate governance context. The diminishing role of Swedish private blockholders and the emergence of an active market for corporate control (which is described further in Ch. 6) have generally been described as reflecting a tax system disfavouring private wealth creation and the growth of collective savings and pension funds. This view is here complemented with a description of the Swedish ownership model as having favoured blockholders in a way that diverges from other countries. It is a governance model that can be described as ownership embedded in a traditional Swedish high trust stakeholder society. In the US and the UK, two countries that just like Sweden feature liquid capital markets and shareholder focus, the boards appear more independent from the (current) shareholders. At the same time the US and the UK system diverge. In Germany, as a contrast, the board has more of a stakeholder perspective integrated into the Companies Act.

Any governance system, embedded in a social system, reflects formal and informal features. In Sweden directors have had to balance a legal separation of control and power with an informal power balance based on societal trust and networks of corporate elites. In financial capitalism this has brought with it new and unanticipated consequences. Institutional investors became an active force on the SSE after the millennium, being very active in the development of the Swedish corporate governance framework. This followed an international trend (Cioffi, 2000), but the special features of the Swedish owner governance gave these institutional investors an enhanced ability to influence the development of the Swedish governance framework compared to institutional investors in other countries. A Swedish board of director in a company with an open and dispersed shareholder structure, i.e. lacking a controlling blockholder, will be more prone to follow interests from current shareholders that take an active position to voice their demands, including asking for share-buy-back programmes, dividend pay-outs and refrain from profit-diluting investments. In short, this board becomes short-termist in its decision-making, driving short-term shareholder value. Shareholder governance is also reflected in the self-regulatory focus of the Swedish governance market where coalitions of actors – such as domestic and foreign institutional investors – can take control of the agenda (Jonnergård & Larsson, 2009).

Summing up, using Sweden as an example this chapter has shown how countries have developed their own systems of corporate governance. In the next section I will show how the choice of governance model has influenced national development of markets for corporate control, and more specifically, cross-border hostile takeovers during the era of financial capitalism.

Chapter 6

A Swedish perspective on takeovers

6.1 Purpose and structure of this chapter

The chapter constitutes the second part of the background studies. The purpose is to show how takeover regulations develop during financial capitalism; i.e. the period that started in the early 1980s and appears to have ended in the autumn of 2008 when the US investment bank Lehman Brothers crashed. Despite certain communality in the adoption of the EU Takeover Directive, nationally diverging company laws and governance traditions make implementation and outcome differ. Therefore, an institutionalist perspective on takeover regulation is foregrounded.

The chapter begins with a description of the Swedish takeover market. Since the 1990s the level of takeover activity on the SEE appears to be interrelated with the change in ownership structure at the SSE during financial capitalism. There also seems to have been higher activity on the Swedish market than in many other countries. This development seems to be partly a result of the Swedish governance model that has enabled shareholders to participate in the takeover process. The chapter then moves on to describe different aspects of the Swedish takeover rules. I reflect on the necessity of specific takeover rules, as part of a specific legal area related to capital markets law and separated from corporate law. I also reflect on the shareholder orientation of the Swedish regulations in relation to the UK and EU. Some of the detected differences between the UK and Sweden relate to diverging approaches to self-regulation. The chapter then moves on to describe the development of Swedish takeover regulation to account for the twin problems of fair and equal treatment of different shareholder groups; i.e. the discussion revolving around a board neutrality rule and a mandatory bid rule. This ends with a description of the Swedish Takeover rules as of 2003, which were in place during the sixth takeover wave.

A last section includes the international scene, relating the Swedish takeover rules to its British and US counterparts, where the latter two diverge both on approach to regulation and to corporate governance. Last, German takeover regulation is described and how it has dealt with that jurisdiction's stakeholder perspective.

The chapter draws on material from a variety of legal documents, including the EU Takeover Directive, Swedish takeover rules as of 2003, statements by the Swedish Securities Council and the Swedish Companies Act. Reference is made to the UK Companies Act, Takeover Panel and Takeover Rules. It also draws on the description of Swedish takeover regulation by Stattin (2009).

6.2 Ownership on the Swedish stock market

The change of the ownership structure on the Stockholm Stock Exchange (SSE) was rather profound during the 1990s, as shown in *Table 7*. In 1992, the year when the Swedish currency regulation was abandoned, foreign ownership on the SSE amounted to seven per cent. Five years later it was around 28 per cent and another five years on it was 39 per cent. During the last five years the percentage has remained stable, between 35–38 per cent.[60] Households' percentage of the total

60 The total wealth in shares in companies listed on the SSE was SEK 3 600 billion at the end of December 2011 (SCB, 2011).

stock market value amounts to around eleven per cent (SCB, 2011). All in all institutional investors of different kinds and nationalities – pension funds, retail funds, sovereign wealth funds and hedge funds – controlled over fifty per cent of the SSE (SCB, 2012). Although part of an international trend the dominance of institutional investors on the SSE has developed further than in many other continental European countries (see Ch. 5.2 and Henrekson & Jakobsson, 2005).

Table 7. Ownership of shares at SSE 1996–2011, by sector (%)

Year	Corporates and Organiz:s	Closed-end Investment funds	Retail funds	Insurance and Life, incl. SNPF	State	House-holds	Non-profit institutions	Foreign owners
1986	17	13	6	19	2	25	10	8
1990	23.4	10.5	8.5	20.4	1.7	18.1	8.5	7.7
1995	10.1	6.7	9.1	17.6	2.9	15.4	7.8	29.6
2000	9.2	6.4	8.5	13.9	4.9	13.1	4.7	39.0
2005	10.8	5.3	11.8	12.2	4.4	14.8	4.8	35.3
2010	11.4	5.4	12.3	12	3.8	13.3	4	37.8
2011	13.8	5.3	11.9	12	3.1	11.2	3.9	38.7

Statistics Sweden (Feb. 2012)

Along with this change of ownership on the SSE there has also been a parallel change of ownership in the Swedish business sector as a whole. A list of the largest listed companies during 1990 still showed a dominance of the two Swedish business groups, the Handelsbank sphere, with its crossholdings with Industrivärden, and Wallenberg sphere, through the investment company Investor and with the family's control established through the Wallenberg Foundation, pyramids and differentiated voting rights. However, by 2000 the Swedish corporate sector had clearly embarked on two different roads. Many of the old large blue chips had been sold to foreign companies. In addition the Wallenbergs had reduced presence on the SSE, partly as the result of the sphere's participation in M&A activities in which the merged entity had chosen to re-incorporate on a foreign stock exchange. In 2007 half of the largest 20 capital owners on the SSE were Swedish pension and retail funds, four were foreign (Nachemson-Ekwall, 2008).

At the same time statistics on takeovers on the SSE show a high level. Changes of control in Swedish companies has actually been as prevalent as in the United Kingdom, generally described as the most liberal capital market in Europe. The SSE's market capitalization as a share of GDP, peaked in 1999, and has since declined (Henrekson & Jakobsson, 2012). A possible explanation for this development might be found when looking into the takeover activities pursued by foreign industrial investors and private equity funds.[61] The number of Swedish hostile bids also increased, including a number of high profile cross-border deals. This followed a US and UK trend, with the overall activity remaining limited but "important" from a financial-theoretical perspective as the activity is presumed to indicate the presence of a well-functioning and efficient market for corporate control (see the theoretical Ch. 2.5).

In 2010, 40 percent of the 500 largest firms in Sweden had their corporate headquarters located outside Sweden (Henrekson & Öhrn, 2011). This change is reflected in the number of Swedish citizens being employed by foreign domiciled companies. In the 1980s about 100 000

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[61] Henrekson & Jakobsson (2012) claim that no corresponding decline can be seen in the UK. Instead, the size of the stock market appears to be relatively constant over time. However, in 2012, there were growing international worry that the public company was loosing attractiveness world wide, in the midst of the financial crisis (see the Economist, May 19, 2012; "Rival versions of capitalism, the endangered public company —The rise and fall of a great invention, and why it matters").

Swedes were employed in foreign controlled companies. By mid 2000 the number had grown to over half a million, almost one of four employees in the private sector (Henrekson & Jakobsson, 2006, 2012; Nachemson-Ekwall, SNS, 2008). In firms with more than 200 employees, 41 per cent of the employees work for firms with at least 50 per cent foreign ownership (Bjuggren & Johansson, 2008).

At the same time the PE industry also appears to have been more important in Sweden than in all other European countries (Kaplan & Strömberg, 2008). Sweden is ranked 5th in the world in PE-market capitalisation, after the US, the UK, France and Switzerland (press release, www.lpx-group.com, September 30, 2010). Several Swedish firms specialize in this sector, managing upwards of SEK 200 billion in 2006 (SCVA, August 2010). Accounting for typical leveraging, this implies a total investment capacity of some SEK 700 billion. In 2010 the level of asset under management had more than doubled to close to SEK 500 billion (*ibid.*). The total number of employees in firms controlled by PE companies in Sweden was estimated to be almost 850,000 in 2011, of which 180,000 were in Sweden (SCVA, 2012). It was estimated in 2011 that close to 7 per cent of business sector employment was in PE-backed companies. The sector's turnover was 8 per cent of GDP.

There are a number of reasons why PE has grown in importance (Jensen, 2007). According to Henrekson and Jakobsson (2012) two aspects stand out as very important in the Swedish context, both related to favourable models of executive compensation, which is particularly important in a highly egalitarian political environment (Roe, 2003; Carlsson, 2007). This is due both to less transparency and possibility of tax evasion as PE funds are legally domiciled in jurisdictions with particularly favourable taxation, i.e. tax havens. To this can be added a generally favourable tax treatment of PE funds compared to other corporate buyers, as well as a tendency from both institutional investors and the financial community to accept higher leverage in companies owned by PE funds compared to publicly listed companies.[62]

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[62] In 2010 and 2011 the favourable tax treatment of the PE-sector in Sweden became a delicate political issue. The debate particularly addressed the role of PE in the pub-

Noting that the Swedish stock market has continued to lose attractiveness to the corporate community after the millennium, Henrekson and Jakobsson (2012) write that a shareholder friendly climate, deregulated capital markets, a new tax regime favouring wealth creation among Swedish citizens and a vital market for corporate control under new takeover rules, appears to have done little to change the trend. Henrekson and Jakobsson also mention that the expected convergence towards the Anglo-American shareholder value regime (as proposed by legal theorists such as Hansmann & Kraakman, 2001) has not happened. As one possible answer Henrekson and Jakobsson (2012) refer to Nachemson-Ekwall (2010); this might be a result of Swedish legal limits as regards to the power of the board of directors during a takeover. Nachemson-Ekwall (2010) writes that the Swedish governance model (described in chapter 5) makes it very easy to take control over Swedish listed firms. Notably a takeover by a PE fund can from a theoretical point be said to resemble a cross-border situation, as the PE fund structure is a foreign legal entity (usually incorporated in tax havens such as the Dutch Antilles).

This moves the description of the (hostile) takeover market to the next section, the development of takeover rules from a legal perspective.

6.3 Takeover rules from a legal perspective

The market for corporate control and cross-border M&A has been influenced by different regulations. I will here mention three aspects related to the Swedish context. First, there is continuous complication between on the one hand takeover regulations, which basically emanate from regulations on listed limited companies originating out of civil law and

lic welfare system and favourable tax treatments from foreign domiciles. It also addressed partner's personal tax, which through the usage of a special fee-structure, 'carried-interest, escaped personal income tax. Se for example Swedish television, SVT, Johan Zachrisson (December 21, 2011). *Sw*: "Friskolor ska inte ägas från skatteparadis".

contractual rights, and on the other hand capital market regulation characterized by a strong focus on liquidity and trading rights of financial instruments. Regulations governing capital markets are found in *the Financial Market Act* (2007) as well as the regulations and guidelines set up by the Swedish Financial Supervisory Authority, SFSA (*Sw*: "Finansinspektionen") and stock market listing rights for corporations.

Secondly, Swedish takeover regulations have developed through the import and implementation of rules from foreign jurisdictions. Cioffi (2000) writes that "(National) legislative and regulatory change has focused on those rules and areas most closely related to the functioning of the securities markets but has left the most basic structural features of the corporate firm intact" (p. 598). Company law, including labour law, has in contrast maintained significant national divergence. From a Swedish perspective this has been documented, inter alia, in Stattin's (2009) analysis of the Swedish takeover rules. As regards Swedish public takeovers, regulation involves a combination of British common law and Swedish civil law. According to Stattin (2009) the influence of British law has made the Swedish takeover regulation more foreseeable as the principles of British common law are more attuned to the needs of the enterprise sector as well as offers a broader scope of cases for legal expertise to relate to. British common law has also influenced EU regulation, making up part of the framework of the EU Takeover Directive (2004).

Thirdly, Swedish takeover regulation struggles to cope with the choice between legislation and self-regulation. Generally takeover rules have been developed out of self-regulation.[63] The most important and possibly the oldest regulation stems from the *British City Code on Takeovers and Mergers*. Sweden is, according to Stattin (2009), probably the country that most resembles UK with its combination of legislation and self-regulation. Continental Europe has another background with a focus on

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[63] For self-regulation to be effective all actors must subscribe to the intention of the rules. In the case of takeover rules this is to maintain trust in the stock market and business sector and from this follows that it is important that the rules are respected by all parties that give advice or in other ways represents a bidding party, the target company or other actors involved in a public bid (Stattin, 2009, p. 103).

legislation (Cioffi, 2000). Notably the US takeover regulation has taken another route partly reflecting variations in state legislation in the area of corporate law (see also sections 6.6 and 6.7).

6.4 The development of the Swedish takeover rules

6.4.1 A British import

In order to understand the development of the Swedish takeover rules I choose to start off in the United Kingdom. The first version of the UK takeover regulation, the City Code on Takeovers and Mergers ("The City Code" or "Takeover Code") came in the 1950s, after a takeover wave when a number of actors were perceived as acting unfairly on the then non-regulated market for takeovers.[64] It was deemed important that shareholders be given enough information to make an intelligent decision and enough time to digest it. From that point the UK principle of shareholder primacy and related board neutrality was established. The UK Panel on Takeovers and Mergers ("The Panel"), an independent body, was established in 1968. The Panel's primary functions were both to issue and administer the Code and to supervise and regulate takeovers. It is a self-regulatory body with the central objective of ensuring fair and equal treatment for all shareholders in takeover bids with the support of transparency rules (for an account of British practises, and the difference between the US and the UK, see Armour & Skeel, 2007).

A central issue for The Panel was the question of introducing a mandatory bid principle (MBR), to enable minority shareholders, in case of the emergence of a controlling shareholder, the right to sell their shares to the same price as had been paid previously. The first version of a MBR was implemented in the early 1970s and has in the UK remained

[64] *The Queensberry rules* (1959) or notes on amalgamation of British business.

rather uncontroversial ever since. These measures were of some help to the incumbent management of a target company confronted with a hostile takeover because, in effect, transparency rules and especially the MBR made takeovers more costly. A "non-frustration" rule, or board neutrality rule (BNR) in the British takeover rule, is found in the London City Takeover Code's General Principle 7 and supplemented by Rule 21 and Rule 37.

In Sweden the self-regulatory body of the Commerce Stock Exchange Committee (*Sw:* "Näringslivets Börskommittée") was founded in 1968 as a joint initiative by *the Federation of Swedish Industries*[65] and the *Stockholm Chamber of Commerce* with the aim of promoting good practices on the Swedish stock market. NBK issued the first takeover recommendations in 1971. These were modelled on the UK Takeover Code with two guiding principles:

- Enable shareholders to properly evaluate a bid.
- Secure equal treatment of shareholders of same shareholder class.

However, Sweden did not copy all aspects of the UK Takeover Code. The rights for a Swedish board to take frustrative actions against a hostile bidder was limited already at the time, as the Swedish Companies Act always limited these rights of the board through the two-tier governance model (described in Ch. 5.3). This included for example the ability to allocate a rights issue to a predestined external party. In Sweden, equity changes have always been an issue for a shareholders' vote at the general meeting.[66] It follows that the UK Takeover Code's board neutrality rule (in the Code's General Principle 7, see here in Ch. 5.3) lacks relevance in a Swedish legal context. At the time in question, a Swedish Mandatory

[65] The federation was merged with the Swedisg Employers' Confeeration (SAF) in 2001 to form *the Confederation of Swedish Enterprise.*

[66] According to the Swedish Companies Act shareholders have preferential rights, emption, to new shares in proportion to the number of shares held (ABL 2005:551, 13 Ch. 1 §§1).

Bid Rule was not implemented as it was seen as conflicting with the blockholder governance structure (e.g. Skog, 1999, for an account).

6.4.2 Diverging British and Swedish self-regulation

The parties involved in the self-regulatory bodies in the UK and Sweden differed. The representatives on the UK panel came from different professions and interest groups such as investment banks and institutional investors. The first Swedish NBK board was made up of representatives from the private industrial sector alone. From the Swedish perspective this private industrial sector covered a number of private owners, many of which had different connections to the two business groups, the Wallenbergs and the Handelsbanken group (see also Ch. 5).

Subsequently Sweden also adopted the UK self-regulatory idea of a more independent panel, which in Sweden took the form of The Swedish Securities Council (*Sw:* "Aktiemarknadsnämnden"). The Council began its operations in 1986 and just like the NBK the initiative came from the Confederation of Swedish Industries and the Stockholm Chamber of Commerce. This body received a broader mandate than the UK Panel from the start. Through statements, advice and information, the Swedish Securities Council promotes good practices on the Swedish stock market in addition to looking after the takeover question. This includes statements in individual cases of compliance with the Swedish Code of Corporate Governance. In relation to the Takeover rules, the Securities Council shall assure that "the rules are interpreted and applied in a manner which is compatible with their aims", (NBK takeover rules 2003, p.1: 2009, I.2, p.7).

Thus, the Swedish system differed from its UK counterpart in that the Swedish takeover rules where issued by NBK and administered by the Securities Council. Since 2005 the Council is one of four organizations that make up the *Association for Generally Accepted Principles of the Securities Market.*[67] However, the separation of the two bodies has been

[67] It is made up of ten bodies, including the Swedish Association of Listed Companies, FAR (the Institute for the Accountancy Profession in Sweden), the Institutional

somewhat illusory, as the directors of the two self-regulatory bodies have been suggested by the same organizations, and there has been a personnel union between the two.

Since it started in 1986 and up until 2009 the Swedish Securities Council has issued around 600 public statements. Two thirds of the statements have addressed takeovers, and the statements in the last years are almost all related to takeovers. To this can be added 2-3 daily consultations, also mainly related to takeovers (SOU 2005:58, p. 58).

6.4.3 Evolving Swedish takeover rules

Since 1972 the Swedish takeover rules have been revised eight times (*Table 8*). In this section the six revisions prior to the sixth takeover wave are addressed. The revisions 2009 and 2012 are described and analysed in Ch. 8: after the three case studies of cross-border hostile takeovers. Just like the British takeover rules the Swedish have evolved as a result of crisis and scandals, i.e. they are path dependent. The *first revision* of the takeover rules was done in 1979, in the aftermath of one of the first modern takeovers in Sweden, Beijer Invests bid on Företagsfinans 1979 (NJA, 1985, p. 343; Ericsson, 1991, p. 8). This was the first time a bid was presented in public without ex ante negotiations with a dominant shareholder group. As such it was the first modern hostile bid too, as it was not well received by the board and executive management of Företagsfinans. The revised rules 1979 included recommendations concerning information on a public offer. Thus, with the Beijer raid on Industrifinans in 1979 Sweden for the first time dealt with a modern takeover bid, defined as a situation where a company publicly asks shareholders in another company to tender their shares on generally stipulated terms. The common procedure has otherwise been to present a bid on a Swedish company after successful price negotiation with a controlling shareholder, which means

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Owners' Association for Regulatory Issues in the Stock Market, Nasdaq OMX Stockholm, the Stockholm Chamber of Commerce, the Swedish Bankers' Association, the Swedish Securities Dealers Association, the Confederation of Swedish Enterprise, and the Swedish Insurance Federation.

that minority shareholders tender in the bid after a large shareholder has already accepted it (Skog, 2003; Burkart & Panunzi, 2003).[68] A *second revision* of the Swedish takeover rules was completed in 1988, in the wake of demands for more detailed information in the prospectus as well as the introduction of complex financial instruments.

Table 8. Revisions of the Swedish takeover rules 1972–2012

Date of Change	Reason
1972	First takeover rules
1979 (revision 1)	Beijer Invest's hostile bid on Industrifinans
1988 (revision 2)	Better prospectus
1999 (revision 3)	Better prospectus and mandatory bid rule at 40 %
2003 (revision 4)	Addressing all listed companies
2003 (revision 5)	Technical revision, MBR lowered to 30 %
2006 (revision 6)	EU Takeover Directive dealt with through *Lagen om Offentliga Uppköpserbjudande (LUA)*
2009 (revision 7)	Major update addressing bidding party, target board and technical issues
2012 (revision 8)	Technical revision

A *third revision* of the Swedish takeover recommendations was done in 1999 with the inclusion of clearer prospectus requirements. For the first time Sweden also introduced a Mandatory Bid Rule (MBR), set at 40 per

[68] Notably this procedure changed after the revision of the Takeover Rules of 2009, when it became common for the controlling shareholder to support an initial bid, which then was contested by a another bidder. See more in Ch. 7.9 analysis.

cent control of stocks or votes. A controlling shareholder above the 40 per cent threshold was to be excluded. By then most European countries had already followed the UK and introduced a 30 per cent cap (Skog, 1999). The opposition from the Swedish community, both from politicians and the industrial elite, had been widespread ahead of the decision.

A MBR was perceived both to hamper restructuring of the Swedish corporate sector and to intrude on the contractual rights for controlling shareholders, as it would be more difficult to sell a block of A shares with voting power above 30 or 40 per cent control at a premium. At the same time, for minority shareholders, often found among institutional investors, a mandatory bid rule in Sweden was welcomed as it was perceived to dampen the sometimes provocative and excessive price differentials between A and B shares. The question of equal prices in a bid offer was also addressed. It was stated that although a price difference was acceptable, the general rule ought to be that the difference should reflect the difference in the trading price on the stock market and shareholders of different classes of stocks be offered the same percentage of price premium. Also, a price difference should not be unreasonable.[69] As a general guideline, the Swedish Securities Council would at the time indicate that a price differential of ten percent would be in accordance with good practice by market actors, but other prices were accepted if individual facts of the case warranted it.

6.4.4 Fourth revision of the Takeover Rules 2003

A *fourth revision* of the Takeover Rules was carried out in 2003, this time in two steps, and it included major amendments (Dagens Industri, Benson, 2003, 15 January). Most amendments addressed issues expected to be included in the anticipated EU Directive. Other amendments targeted specific Swedish problems. This included the private equity firm Industrikapital's failed bid on Perstorp in 2000, which had been an issue for

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[69] For a general discussion of what an appropriate price difference might be see statement from the Swedish Securities Council (AMN 1989:7) in connection to the Gota Bank bid on Wermlandsbanken.

the Securities Council to handle (AMN 2000:20). The major amendments were:

1. The rules apply to all bidding parties on the stock exchange, not only to Swedish listed companies.
2. It must be clear that a bidder has proper financial support for the bid.
3. The conditions set up for the fulfilment of the bid must be objectively assessable. A bid can only be withdrawn if the level of acceptance does not reach a predefined target, if a better offer is presented or any other criteria of major importance is not fulfilled (such as competition clearance).
4. The acceptance period must be no less than three weeks.
5. The offer is binding.
6. The offer may not be lower than the highest price the bidder has paid for stocks six month before the public offer and nine month thereafter.
7. If the bidder buys ten per cent of the shares during the offer period, other shareholders must also be offered a cash settlement on equal terms.
8. The board of directors should be more restrictive as regards due-diligence procedures. A bidder is not allowed to trade in the share during a due-diligence process and all price sensitive information must be made official.

Most of the amendments to the NBK Recommendations (2003) aimed at strengthening the position of target shareholders. It was restated that the board of the target company might not take frustrative actions without the clearance of the general meeting, but for the first time a shareholder focus on the board's role during a takeover was specified, albeit only in general terms. NBK II.14 (2003) includes a new statement that the board of directors shall present its view on a bid, and reasons for this, in time for shareholders to make a qualified decision on which action to take. It states that the board should act in the interest of all shareholders."…This means that that the board might not in its decision be governed by the interest of a specific shareholder or group of shareholders and not of the board's own position..." (NBK 2003, p. 21)

Another novelty in 2003 was that thereafter three representatives from the institutional investors were to be on the NBK board, thus moving the Swedish takeover panel closer to its UK counterpart as far as the characteristics are concerned.

The takeover rules were amended again in September of 2003, the *fifth revision*. One addition was that a bidder must include into the bid a statement that it planned to comply with the recommendations in the takeover rules and the Swedish Securities Council's interpretation of them. The other was a decision to lower the threshold for the Mandatory Bid Rule from 40 per cent to 30 per cent to align Swedish procedures to other European countries that at the time had almost all settled for a 30 per cent level. This time exceptions to the MBR were to be limited to shareholders that before 1 July 1999 already were in control of 40 per cent of the shares. Shareholders with ownership between 30 and 40 per cent, however, would be forced to comply with the MBR and thus were not able to increase their shareholdings.[70] At the time, this group included for example German vehicle conglomerate VW's 34-percent shareholding in the truck company Scania. The Swedish takeover rules also changed name to Swedish Rules of Public Offers Takeovers, (*Sw:* "Regler rörande offentliga erbjudanden om aktieförvärv"). Summing up the Swedish takeover regulations as of the fifth version 2003, there had by now been a shift away from the one-sided ability of incumbent blockholders to dictate the construction and pricing of an offer and a strengthening of the role on the stock market of minority shareholders, such as institutional investors.

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[70] Among actors excepted from the MBR were (SIS Ägarservice, 2003) because ownership surpassed 30 per cent were the Wallenberg foundation (Investor), family Persson (Hennes & Mauritz), family Wallenstam (Wallenstam), Söderberg foundation (Ratos), family Paulsson (Skistar), family Douglas (Latour), family Bennet (Elanders) and the Stenbeck foundation (Invik).

6.5 Takeover directive and Swedish regulation

A common EU platform for takeovers was introduced in 2004, with the adoption of the Takeover Directive (*Sw*: "Europaparlamentets och rådets direktiv 2004/25/EG av den 21 april 2004 om uppköpserbjudanden"). In accordance with the Takeover Directive, the Swedish Financial and Supervisory Authority, SFSA, has since 2006 overseen the implementation of this directive along with a number of other directives such as the Prospectus Directive and the Transparency Directive. However, Nasdaq OMX Nordic Exchange Stockholm is responsible for the supervision of the takeover rules and also monitors market activity. The two institutions, SFSA and Nasdaq OMX, have delegated supervision of the Swedish Takeover Act (*Sw:* "Lagen om offentliga uppköpserbjudanden på aktiemarknaden"), (2006:451) ("LUA") to the self-regulatory body Swedish Securities Council that rules on exemptions. Parties can appeal to the SFSA. [71]

The Directive, *the 13th Company Law Directive*, was modelled on the UK system, just like the Swedish takeover rules has been. The Directive can be seen as minimum requirements and individual EU members may well have stricter and more detailed regulation (SOU 2005:58). At the same time, in cases were local regulation do not give enough guidance, such as the Swedish NBK-rules, the Directive will apply with direct effect.

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[71] The SFSA has delegated to the Swedish securities council the duties referred to in Ch. 7:10 of the Act on public takeover offers on the stock market (FFFS 2006:4). This means it is incumbent upon the council to rule on the following issues cited in the act: a) extensions of the time limit to prepare and apply for approval of offer documentation (Ch. 2:3 §2) b) whether a mandatory bid must be offered by a party closely related to the bidder (Ch. 3:4) c) whether a mandatory bid applies according to the provisions in Ch. 3 of the Act (Ch. 7:4) d) whether a particular action conflicts with the provisions on defensive measures in Ch. 5 of the Act (Ch. 7:4) e) exemptions from the provisions on mandatory bids (Ch. 7:5) f) exemptions from the provisions on defensive measures (Ch. 7:5).

The delicate some twenty-year battle that preceded the introduction of the EU Takeover Directive has been described by a number of academics (Skog, 1997; Berglöf & Burkart, 2003; Kraakman & Hansmann, 2009). Hopt (2002; p. 3) writes that the "Legal and political process has been long, complicated, and painful". Enriques and Gatti (2006a) were no less expressive with their comment that: "What remains of the Takeover Directive is a patchwork of mandatory rules, possible waivers, and optional provisions, which still attempts to emulate as closely as possible the British model of takeover regulation" (Enriques & Gatti, 2006(a), p.18).

In the initial work with the directive the idea was that the risk for different stakeholders, in removing existing barriers to enable cross-border hostile takeovers, was to be minimized by legal protection of minority shareholders and also of for example employees. However, during the process a number of countries objected to the Directive, worrying that the directive would not adequately tackle the problem of a level playing field for takeover defences within Europe and between the EU and the US. One of the more vocal critics was Germany (see also Ch. 6.8).

This controversy, related to board neutrality, the responsibility of employees and the right for shareholders to decide, is reflected in the directives central General Principles, Article 3:

> (b) The holders of the securities of an offeree company must have sufficient time and information to enable them to reach a properly informed decision on the bid; where it advises the holders of securities, the board of the offeree company must give its views on the effects of implementation of the bid on employment, conditions of employment and the locations of the company's places of business;
>
> (c) The board of an offeree company must act in the interests of the company as a whole and must not deny the holders of securities the opportunity to decide on the merits of the bid. (Takeover Directive, 2004/25/EC, p.15)

The topic of Article 3 is further addressed in the Takeover Directive Article 9, dealing with frustrative actions or board neutrality, which requires that once a bid has been communicated, target shareholder approval must be obtained for the taking of any defensive action not already implemented (other than the solicitation of rival bids). Article 9 carries a wording close to what is found in the UK Takeover Code (2009). The BNR gives the UK board some rights to search for a white knight or present a defence document. From a Swedish perspective, this board neutrality of the Directive was not controversial as the Swedish Companies Act already solicited the board to act in the interest of the shareholders and this fiduciary role was enforced in the revised NBK rules 2003.

The other controversial topic in the Takeover Directive addressed Article 11 and the so-called "breakthrough-rule". This article has received more interest from the Swedish business community. It governs break-through of certain restrictions on transfers and voting rights in a takeover situation. It states that any defence measures used in Article 9 falls once the bidder achieves 75 per cent of the target's voting power, and a bidding party can then assemble a shareholder's meeting for the purpose of altering the constitution to remove these provisions permanently. Article 11 challenges the regime of differential voting power among shareholder classes.

A political compromise amongst European politicians on this delicate issue, as discussed previously, was reached whereby Article 9 and Article 11 became optional (stated in Article12 in the Takeover Directive of 2004). If a member state does not apply them, target companies can themselves voluntarily submit to the provisions through a shareholder resolution. This has not been done in any Swedish listed companies as of 2012. Member states that do implement Article 9 and Article 11 for their registered companies can allow a subsequent disapplication of them for any particular bidder that is not (or whose controlling stockholder is not) subject to those articles.[72] Despite this apparent setback for the Commis-

[72] This means that any EU cross-border acquirer that is not subject to Article 9 and 11 provisions in its home state, and U.S. and other non-EU acquirers, may face continued use of board-instigated and other structural defences. In a scenario with com-

sion the work with the takeover directive did create a more level playing field. For example, the issuing of golden shares by member states to limit unwanted shareholder influence, deemed illegal by the European Court of Justice, targeted France, Portugal and Spain (Hopt, 2002). The Directive also includes a Mandatory Bid Rule, as to allow shareholders an option to sell in cases of a change of control (EU Takeover Directive 2004/25/EC, 5 §).

Sweden implemented the Takeover Directive on 1 July 2006 through the Takeover Act or "LUA" (above). This did not result in an actual revision of the NBK (2003) takeover rules, but for pedagogical reason I have chosen to call it a sixth revision as the legal interpretation of the NBK rules were changed. Some areas that had previously been dealt with by NBK through self-regulation, moved into legislation through LUA. This included flagging requirements. Rules on the disclosure of major shareholdings through flagging, however, are addressed in the Financial Instruments Act, based on another directive, the EC Transparency Directive (2004/109/EC) implemented in Sweden on April 1st, 2007. When LUA was implemented Sweden chose to *opt-in* on the Board Neutrality Rule, Article 9. Sweden chose to *opt-out* on the Break-through Rule, Article 11.

With the implementation of the Takeover Directive the MBR was changed once again. LUA took care of mandatory bid requirements in the case of a shareholder surpassing 30 per cent of voting or capital control (LUA 3:1). Shareholders already in control of more than 30 per cent of votes were exempted. This meant that the NBK 2003 recommendation of special treatment of shareholders in control of blocks between the 30 and 40 percent, which was the target from 1999, remained.

> "We propose that the legislation shall not include an equivalent rule of transition; rather a shareholder that at the time of the implementation already controls 30 per cent of the votes should be able to increase its shareholding without breaching the mandatory bid at any level. A codification of the

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peting bids, there can be inequality of treatment of rival bidders where disapplication is permitted against one bidder but not the other.

> NBK's transition-rule might be regarded as a breach with the Directive and within all circumstances be difficult to explain and defend to the rest of the world" [73]

At the same time, Sweden did not follow the example of many other member states to introduce additional thresholds above that 30 percent level.[74] Section 10 of the Swedish takeover Act, LUA, stated: "The obligation to make a bid to all the holders of securities should not apply to those controlling holdings already in existence on the date on which the national legislation transposing this Directive enters into force."

As a result the Swedish takeover market, at the time of the sixth takeover wave had to comply with three regulatory frameworks – The NBK Takeover-rules (2003), the Takeover Directive (2004/05) and the then anticipated Swedish Takeover Act (LUA, 2006). To this could be added a number of other legal requirements, including the Swedish Companies Act.[75] What this might imply for different constituents involved in a cross-border hostile bid is the focus of Chapters 7 and 8.

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[73] Ministry of Justice, proposal referred to the Council on Legislation for consideration (*Sw:* "Lagrårdsremiss") Bodström and Danielius, (2006) *Sw:* "Offentliga uppköpserbjudanden på aktiemarknaden", February 9.

[74] Finland settled for a 30 percent trigger as well as a 50 per cent trigger, Denmark and Italy apply a 33 per cent threshold and a 50 per cent threshold. Norway let companies from EU members comply with their domestic thresholds. For domestic companies and companies outside EU thresholds are set at 33 per cent, 40 per cent and 50 per cent.

[75] There is also the Swedish Companies Act (ABL 2005:551), which contains the rules governing the compulsory acquisition of minority shares and statutory mergers. The Takeover Act also demands that a bidder presents an offer document containing all information necessary for a comprehensive assessment of the bid, including both cash and share offers. These rules are included in financial instrument trading act (Lagen 1991:980 om handel med finansiella instrument) and also with rules included in the EU prospectus regulation, introduced in Sweden as of 1 January 2006 (Commission Regulation 809/2004 of April 29, 2004).

6.6 Relating to Anglo-American regulation

There are important differences between the US and UK market during a takeover. This is due both to differences in regulation and to different approaches to corporate governance. Despite communality in company case law, the UK has settled for self-regulation and codes involving market actors whereas the US has chosen the legal track with a focus on the business community. There are historical explanations for the difference, which can be summed as strong presence of institutional investors in the UK and a dominance of management in the US (Cioffi, 2000; Armour & Skeel, 2007; also chapter 3.4.1). In the UK, self-regulation was pushed forward by a community of investment bankers and institutional investors, all of who regularly interact in the City of London. In the UK corporate managers were not a well-organized constituency and UK management felt dependent on their City advisors to maintain a good relationship to investors (Armour & Skeel, 2007).

In the US on the other hand, federal regulation in the Depression era of the 1930s restricted both the scale and the scope of services that financial institutions were permitted to provide, crucially undermining the ability of institutional investors to coordinate. This led to less institutional ownership than in the UK and hostility towards self-regulation (Armour & Skeel, 2007). This explains the political and legal reaction to the hostile takeover boom of the 1980s that generated anti-takeover laws and anti-takeover devices that effectively restored much of the managerial power of the status quo ante (Cioffi, 2000; p. 588). The result was that a wave of anti-takeover statutes in the late 1980s and early 1990s weakened US-shareholder supremacy and the US-market for corporate control.

The United States adopted takeover regulation, *the Williams Act*, in 1968, the same year as the UK. It addresses tender offers with the aim of protecting and guaranteeing both equal treatment of all shareholders with respect to information and assure that incumbent shareholders were protected from under-priced sales of shares. Thus, in effect, rather than supporting the exit of shareholders, as the British takeover regime does, the US regulation encourages shareholders to stay invested in the target company (addressed in chapter 2.5 on the difference between Berle & Means, 1932/1968 and Manne, 1968). The US takeover regulation has instead focused on developing minority shareholder rights.

The Williams Act also differs from the UK Takeover Code in the sense that it does not take a stand on management's role in the acquisition process. Rather the Williams Act seeks to provide the offeror and target management equal opportunity to present their cases to incumbent shareholders. The management's role was highlighted in the wake of a wave of hostile takeovers in the late 1970s and early 1980s. After protests from the business community numerous states, including ware, granted the management protection in the form of anti-takeover statutes and bid-frustrating defensive actions. This approach is more or less the opposite of the British approach; as a consequence, the decision in the US about the change of control rests to a large extent with the management and not with the shareholders as in the UK. The protection of minority shareholders is in the US in some way guarded by regulations stipulating that a new controlling shareholder register its intentions with the Securities and Exchange Commission (the 13D-filing). This includes any shareholder in control of over five per cent of capital and votes.[76] Both the UK and the Sweden takeover rules (as well as the Directive) lack equivalent requirements.

The state of Delaware, where most large listed US companies are incorporated and courts have a developed body of case laws to judge on business matters, allows directors to take action to fend off a bid as long as it is in line with their fiduciary duties to act in the interest of the company. Director's fiduciary duties are regulated in the Business Judgement Rule (BJR), which does not have an equivalent the British or Swedish

[76] The statement in the 13D-fling includes information of the Purpose of Transaction – This allows the public to see why an actor is buying shares in the company, whether it be for acquisition, hostile takeover, proxy war, or simply because it believes the company to be undervalued. The actor has to bring forth an explanation.

corporate law.[77] Within the BJR a US director has to be able to demonstrate arguments showing the reasonableness for a stand on an offer before being protected by the business judgment rule (Cieri et al., 1994, referred in Johnson, Daily & Ellstrand, 1996)[78]. This includes being able to claim that it might be ambiguous which decision will maximize shareholder wealth, but employees and other stakeholders could be harmed if the bidder was to succeed. Delaware corporate law also allows change of control-clauses in executive compensation programmes to enhance the management's will in making an independent and proper judgement.

Also, during a control fight a US board is in a stronger position than the British or Swedish boards. It controls director enrolment both through proxy voting and overlapping tenures, making it difficult for a hostile party to exercise power while at the same time offering the incumbent board certain time to take actions that will increase the chances of the company surviving as an independent entity long term.

The more elusive question is of course which of the two systems, the UK or the US, is the most welfare accretive for society at large. Both systems appear to be equally deal-driven. The British mandatory bid rule and the British board neutrality rule may be regarded as distortions of a more efficient market mechanism. However, neither limitation appears to have inhibited directors and executive management involvement in the takeover process nor do they appear to have prevented control

[77] Directors' fiduciary responsibility is evaluated by US courts on the basis of the Business Judgment Rule, which presumes action taken in good faith, in the best interest of the corporation and that directors be disinterested and independent. Two court cases decided in the 1980s, Unocal and Revlon, identify two different ways in which Delaware's modified Business Judgment Rule is applied. Svernlöv (2007) offers a comparison of the business judgement rule, the Delaware corporate law and the Swedish board's Duty of Care (ABL, 2005: 551, p. 136).

[78] Cieri, R. et al., The fiduciary duties of directors of financially troubled companies, 3 J. BANKR. L&PRAC. 405, 406 (1994) ("The duty of care requires that directors act in an informed and considered manner, meaning that prior to making a business decision, the directors must have informed themselves of "all material information reasonably available to them" and, "… having become so informed, they must then act with requisite care in the discharge of their duties."), quoting Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984).

transactions from taking place. A prerequisite for this success appears instead to be British regulatory disfavour of controlling shareholdings. British corporate governance makes it difficult for a blockholder to control the board of director even with a large shareholding. Considered a stakeholder, a large shareholder is prevented from dominating the board of directors. The UK listing rules dealing with related party transactions prevent any shareholder, or related party, accounting for more than ten per cent of voting rights from casting his vote at the general meeting, in the presence of a conflict of interest over a significant transaction. This includes parent-subsidiary mergers and similar changes. The effect of this is that it is very difficult for an external party to get full control. The acquirer would not be able to merge the target company into his own, unless a super-majority of the non-tendering shareholders consent, and the presence of minority shareholders would make him subject to all the restrictions of decision rights faced by a controlling shareholder.[79] In this respect the contrast to Swedish controlling shareholder supremacy is quite stark.

US regulators have no such preference for dispersed shareholders. US corporate governance allows both shareholder control and dispersed shareholdership. However, it is difficult (impossible) for ordinary shareholders to nominate directors, as it is the board and executive management that control the proxy voting. The US does not regard a controlling shareholder as a problem at all. Pacces (2007) writes that "Both courts and commentators tend to regard sales of control blocks on the free market as transactions that are normally beneficial to minority

[79] Related party transactions and voting are addressed in UKLA Rules 11.1.8, FSA Handbook, www.londonstockexchange.com; Based on Listing Rules (LR) §11.1.7, related parties and their associates cannot vote on the shareholder resolution approving the company's transaction with them. According to LR §11.1.4 a substantial shareholder qualifies as related party. "Substantial shareholder" is defined in LR, Appendix 1, Relevant definitions, as "any person (excluding a bare trustee) who is entitled to exercise or to control the exercise of 10% or more of the votes able to be cast on all or substantially all matters at general meetings of the company. Pacces (2207) offers an account of the implication for blockholders' lack of interest in controlling British listed companies.

shareholders, in that they essentially feature an efficient dynamics of control allocation." (p. 726). The case is that Delaware corporate law rather encourages minority shareholders to stay on, protected by strong minority rights (Pacces, 2007). However, the SEC 13-D-filing in the US, mentioned previously, limits the controlling shareholders ability to sell its shares to just anyone. Pacces (2007, p. 726) writes: "The controlling shareholder is not allowed to sell to a looter. This may seem rather obvious in cases of outright fraud, but the transaction may be also challenged on grounds of gross negligence or misrepresentation of material facts." Although no such restriction exists in Sweden (where anyone can own a large block of shares but some limits are put on the enrolment of directors), this US view has had much in common with the Swedish owner perspective and strong minority rights.

The role of the management board of a target company in a US bid fight can also be discussed from another perspective, that of the bidding company and its relation to its shareholders. Since the US takeover-regulation has granted the management board a certain amount of bargaining power to counteract a bid from a party perceived to be hostile, the risk is that a US bidder ends up paying higher prices during a takeover than in a UK takeover. This is of course in the interest of the selling shareholders but not necessarily in the interest of the buying shareholders. It could be argued that in the US where the shareholders of a bidding company, lacking voice, more often risk ending up as owners of shares in a company where the management, out of self-interest, paid too much in a transaction (which is also suggested in financial literature where as much as 2/3 of all public takeovers end up as value destructive).[80]

[80] There are arguments that Europe should go for a Business Judgement Rule rather than a Board Neutrality Rule as to strengthen incumbent boards bargaining power (Kirchner & Painter, 2000).

6.7 Relating to German regulation

Public takeovers were an exception in Germany until the late 1990s. Hostile takeovers were practically unheard of. The first German takeover guidelines that targeted the rights of minority shareholders were introduced by the Kohl-government in 1989, the Takeover Code (*Gr:* "Übernahmekodex").[81] This recommended equal treatment of shareholders. However, the Takeover Code was non-binding and did not provide for any sanctions, and not all companies signed the voluntary declaration to follow it. Also, the code did not address the management board's usage of poison pills to prevent unfriendly bidders nor address private offers of less than 50 percent of the stocks. Thus, Germany, with its strong stakeholder tradition, represented for many years an exception to the Continental European convergence toward the UK system of takeover-regulation.[82]

Around the millennium, German politicians and businessmen were strong opponents of the EU adoption of the 13th Takeover Directive. The critique addressed in particular the plans in the directive to include binding non-frustration rules and the implicit risk that these would lead to an uneven playing field among the constituents involved. The fear was that this might lead to German corporations being more vulnerable to hostile acquisitions from bidders located in other countries.

However, Germany did not remain totally insulated from foreign pressure to open up the German takeover market. In 2000 British mobile phone group Vodafone made a high-profile cross-border hostile takeover of the German conglomerate Mannesmann, at the time the largest hostile bid on a European listed company.[83] Germany enacted a new takeo-

[81] More exact: "Übernahmekodex der Börsensachverständigenkommission beim Bundesministerium der Finanzen of 14 July 1995, amended 1 January 1998"; see Schuster/Zchocke, Übernahmerecht / Takeover Law (1996).

[82] For an account on German Takeover regulation see Cioffi (2002), Gordon (2002), and Hopt & Leyens (2004).

[83] Höpner & Jackson (2001) provide detailed overview and analysis of the Mannesmann takeover and its implications for German corporate governance.

ver law in 2002, WpÜG, (*Gr*: "Wertpapiererwerbs- und Übernahmegesetz", which eliminated takeover defences such as differential voting rights, voting caps and cross-shareholding. The WpÜG is structured like the City Code but otherwise a legal document implemented by a government agency, the Federal Financial Supervisory Authority. All decisions can be challenged in court and this is commonly used, making takeovers, friendly as well as hostile, long and costly to the bidding party. The German takeover law of the WpÜG complies with the Takeover Directive's equal treatment of shareholders and offer transparency levels which are in line with international standard. This included the adoption of a MBR set at 30 per cent, in the absence of a different de facto controlling shareholder.

Like many European countries Germany experienced high takeover activity during the sixth takeover wave. Still, it is clear that German takeover rules differ from the rest of Europe's in general and from Sweden's in particular. The German board's primary legal obligation is to act in the best interests of "the corporation as such", which means in the best interests not only of shareholders, but also of other stakeholders such as employees. The German Takeover Act (WpÜG, General Principles, 3:2) also states that: "The board of management and the supervisory board of the target company must act in the interests of the target company." Given this starting point the WpÜG offers management and the supervisory board certain freedom to take action to fend off a hostile bidder. In the Takeover Directive, Germany has opted out on both Articles 9 and 11. For companies that have chosen to comply with Article 9 there is also an option to demand reciprocity.

A German management board can take a number of actions with the approval of the supervisory board alone. This includes disposal of important company assets ("sale of crown jewels").[84] Given that half of

[84] Other examples are the creation of antitrust issues, change of the financing structure, counter-offer to the takeover of the bidder ("Pac Man" offer), severance payments for members of the management board ("Golden Parachutes") or agreement on change of control clauses.

the supervisory board is made up of employee and union representatives, and that the independent directors likely have relations with management, the chance that management will obtain support is quite high. There are also complications for a bidder that has not gained full control to get access to the supervisory board, including limited rights for individual shareholders to nominate members of the supervisory board and staggered terms of office for the members of the supervisory board. Even in the case of a "friendly" takeover the board of both the acquiring corporation and the acquired corporation have wide discretion to decide which business combinations are appropriate. This means that the employee-directors of the target company will have a say on jobs and factory shutdowns (Hopt, 2011).

6.8 Conclusion

Sweden has experienced an active takeover market in financial capitalism, second only to the UK market. But there are differences between the Swedish and the British takeover market. Swedish takeovers have often involved a foreign bidder, and this has largely transformed the control of the Swedish corporate sector since the 1990s. Sweden has also experienced a higher number of PE takeovers relative to GDP than most European economies. A number of explanations have been offered with taxation issues most prevalent in the literature. In this chapter, however, the discussion has been complemented with a description of how takeover regulation has been implemented in the Swedish corporate-governance context.

Takeover regulation was adopted in many countries during the late 1960s. Although introduced to enhance the activity of the market for corporate control and perceived to be a wealth accretive mechanism (as it facilitates restructuring), the way it has been implemented in different nations and what issues it has addressed reflect features specific to each. Among these features are domestic responses to previous economic crises (such as the Great Depression or Enron crash in the US or the Krueger crash in Sweden), the growth of institutional investors (that began earlier in the UK than in the US), the choice between self-regulation and legislation (depending on the distribution of power among market participants, corporate management or owners of the corporations) and the role of employees (which is present in the German corporate charter). The Williams Act in the US, the Takeover Code in the UK and the EU Directive on Takeovers and Mergers all reflect the bargaining power of interest groups (i.e. elites). In the same vein, Swedish takeover regulation reflects a web of international and national legislation and self-regulation, with elements of local norms and cultural tradition. This has not been done without complications:

- Sweden has introduced *one set* of regulations – disregarding the ownership structure.
- Sweden has leaned heavily on the UK board neutrality rule, which makes the incumbent shareholders rather than management the supreme decision makers during a bid.
- Sweden has had difficulty coping with the Mandatory Bid Rule, as it limits the power of incumbent block owners.
- A number of deals have experienced complications due to the treatment of A and B shares during a bid.

This means that the Swedish takeover market has come to differ in certain aspects to the UK, US as well as German takeover markets. Using a Swedish perspective the EU approach to creating a "level playing field" among corporate actors across Europe seems not to deliver expected outcome. Instead, the three hypotheses summarizing the theoretical chapter 3.6 may from a Swedish perspective be redefined and transformed into three new hypotheses:

> *Swedish hypotheses 1:* The Swedish corporate model of owner governance has difficulties in its quest to balance the value accretive strategy of a board and management with financial capitalism's one-sided preference for (current) shareholder value and liquidity over more stakeholder-oriented governance models.

> *Swedish hypothesis 2:* In Sweden a strong presence of institutional investors investing according to portfolio theory and with a preference for shareholder-value governance pushes corporate directors and management towards short-term strategies and facilitates cross-border hostile sell-outs.

> *Swedish hypothesis 3:* The Swedish version of liberal, open and liquid capital markets with globally active institutional investors will lose out to actors from national regimes that are more protective in their company law, governance systems and takeover regulation. This is reflected through arbitrage, both regulatory and morally.

What this might entail for Swedish companies with a dispersed shareholder structure targeted in cross-border fights is illustrated through the empirical case studies of Skandia and Capio. The implications for a company with a traditional blockholder structure, is illustrated by the Scania contest. These studies are addressed in Ch. 7. The analysis of the three case studies is related to the revision of the Swedish takeover regulations 2009 in Ch. 8.

Chapter 7

Three case studies

7.1 Purpose and structure of this chapter

This chapter consists of three empirical, longitudinal case studies of cross-border hostile takeovers involving Swedish targets during the sixth takeover wave. The purpose is to develop the three hypotheses from chapter 6.8 addressing a corporate governance process in financial capitalism. These hypotheses address the Swedish corporate model of owner governance (hypothesis 1 in Ch. 6.8), the role of institutional investors as corporate governors (hypothesis 2 in Ch. 6.8), and actors' ability to pursue arbitrage, both regulatory arbitrage between different soft and hard laws and moral arbitrage, relating to cultural and historical differences (hypothesis 3 in Ch. 6.8).

The case studies are South African-British Old Mutual's hostile bid on the insurance company Skandia 2005, the PE bid on health-service provider Capio 2006 and German MAN's (and VW's) hostile bid on the heavy truck producer Scania 2006. Taking a sociological and institutionalist perspective, the case studies reflect takeover-processes essentially influenced by three "forces" - actors, institutions, and culture. Seen together they highlight the interplay between national regulatory regimes, power elites and actors' personal preferences for abetting or obstructing a bid. As a result these three power struggles appear not to have taken place on a financially efficient market for corporate control (Manne, 1965). Rather, the case studies illustrate how the Swedish (shareholder friendly) model of corporate governance is exposed to a bricolage of features and actions related to rationalities of global actors in financial capitalism in which the adoption of British governance principles into a Swedish setting plays a primary role.

Especially interesting in this process is the double-edged fiduciary role of the directors. They are obliged both to a) follow rules to guard the company according to the Companies Act and b) act as agents of the shareholders in accordance to capital market regulation, implying e.g. taking a neutral stance during a bid.

All hostile-bid processes are different and forces influence the outcome of each hostile-bid in different ways.[85] In the Skandia study, the takeover process involves a corporation with a dispersed ownership structure and thus resembles a Fama and Jensen (1983) agency conflict. However this fight for corporate control does not match the US dispersed Berle and Means (1932) shareholder common in the US but involves actors in British and Swedish governance regimes. The smaller Capio study can in many ways be described as a ”hyper” Skandia as that hostile takeover process involved a target company with a dispersed shareholder structure and covered only a period of two months. Many of the actors involved modelled their actions on the Skandia process. The third case study, Scania, addresses a cross-border hostile bid targeting a company embedded in a Swedish blockholder structure with A and B shares. As such the Scania case also features a conflict involving the relationship between a controlling shareholder and minority shareholders, i.e. a principal-principal conflict and also includes aspects of the free-rider dilemma (Grossman & Hart, 1980, 1988). The Scania study offers rich material on possible regulatory arbitrage when actors subscribe to different governance regimes and respond to different regulatory settings (e.g. German stakeholder governance).

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[85] It is tempting to quote the first line in Lev Tolstoy's late 1800-epos Anna Karenina; ”Happy families are all alike. Every unhappy family is unhappy in its own way”.

The rest of the chapter is structured as follows: Each case study is described individually (Sections 7.2; 7.4; 7.6). They are presented as narratives with background and a description of the takeover process along a time line. Each case ends with the completion of the hostile bid. After each case follows an analysis related to the propositions developed previously (Sections 7.3; 7.5; 7.7). The methodology behind the three case studies has been outlined in chapter 4 and in the Appendix. Here it is sufficient to say that the Skandia case is based on in-depth interviews with well over a hundred persons, which enables a unique and detailed reconstruction of the forces and rationalities of actor's activities, including the board of directors. The Capio study is based on media reports, a small numbe rof interviewes and is more limited in both depth and scope. It will be approached as a complement to the Skandia study. The Scania study compiles almost fifteen years of media reporting and other public material. The focus on regulatory arbitrage in the Scania case has made it necessary to include a description of German corporate governance at the relevant time period. The three cases constitute material referred to in the amendments to the Swedish Takeover Rules 2009 (dealt with in Ch. 8).

7.2 The Skandia case[86]

7.2.1 Background

On 2 September 2005, London-listed financial conglomerate Old Mutual (OM) presented a bid on Stockholm-listed insurance company Skandia. On 14 February 2006, OM declared control of Skandia, against the recommendation given by the majority of the Skandia board. Thereby, OM had completed a "hostile" takeover of a corporation that had long

[86] This empirical part is based on material found in *Corporate Governance in Financial Modern Capitalism; Old Mutual's hostile takeover of Skandia* (Kallifatides, Nachemson-Ekwall & Sjöstrand, 2010).

been in the hands of a broad spectrum of Swedish and foreign institutional investors (see footnote 86). The deal had spurred much public upheaval and received heavy media coverage, as it had split the board into two opposing groups for and against the bid, with the chairman recommending the bid against the wishes of the CEO. The deal also revealed both conflicting and contradictory actions within Skandia's dispersed group of institutional investors and had shed light on dubious activities by middlemen such as investment banks, lawyers and media.

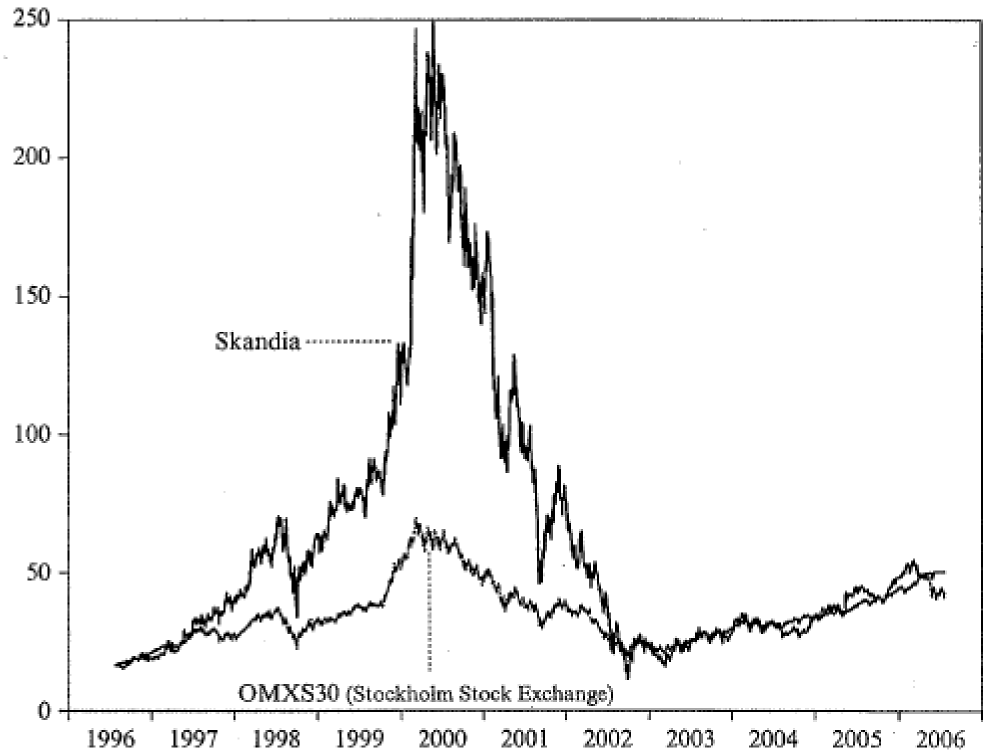
The process leading up to this conclusion had been long and delicate. Listed since 1863, Skandia had together with its mutual life arm Skandia Liv, been the largest Swedish private insurer with a property & casualty business and a major investor on the Stockholm Stock Exchange. From a governance perspective Skandia was an example of managerial control, in this case as a result of restricted voting rights. Due to Skandia's importance at the time, as it had shareholdings in a number of large Swedish listed companies, members of the Swedish business elite were always present on the corporate board.

During the 1990s Skandia converted from a traditional life and property & casualty insurance company to a focus on unit-linked life insurance.[87] Skandia expanded abroad, being especially successful in the US and the UK. A new management team adopted, with the support of a passive board of directors, a US-oriented shareholder-friendly model of corporate governance, including an agency-theory inspired focus on executive compensation programmes involving bonuses and stock options. At the same time shareholder power was enhanced when voting restrictions where abandoned in a number of steps. This was well received by investors and Skandia shares skyrocketed (*Figure 10*). In March 2000 – at the peak of the IT-bubble – Skandia had a market value of SEK 250 billion (approx. 250 SEK per share; GBP 18 billion); valued more than twelve times the book value of equity. After the IT crasch 2001 – with Skandia valued at SEK 11 billion – it became apparent that Skandia's

[87] A thorough account of the "Skandia crash" is offered in Nachemson-Ekwall & Carlsson (2004).

business model had faltered, revealing distortive accounting practises, hefty bonus pay outs to top executives and possible management fraud.

Figure 10. The Skandia share



Kallifatides et al. (2010)

The US subsidiary American Skandia, previously perceived by the stock market to be worth over hundred billion SEK, was sold at a loss. Skandia was seen as the Swedish equivalent of Enron.[88] In 2003, Skandia's CEO

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[88] Enron crasched in 2001 and was the largest US corporate scandal that emerged in the aftermath of the dotcom-bubble crash. It contributed to the introduction of Sar-

and chairman were replaced along with many other directors and managers. Legal disputes emerged in many areas.

Table 9. Skandia's ownership structure

Shareholders	December 2000 (%)
Foreign investors	56
Pohjola Group	10.5
Industrivärden	4.8
Robur Funds	3.3
AMF	2.5

Shareholders	July 2003 (%)
Pohjola Group	9.0
Sampo	6.9
Industrivärden	4.8
Alecta	4.1

Shareholders	March 2004 (%)
SEB Funds	4.2
Swedbank Robur	3.9
AP2	2.5
SHB Funds	2.4
Singapore	1.7
Alecta	1.4
Nordea Funds	1.3
AP4	1.1
AP1	1.1
Fidelity Funds	0.8
10 Largest	20.4
Market value	30 Billion SEK

SIS Ägarservice (2000–4)

It may be noted at the outset that both Finnish Sampo, with earlier ambitions to acquire Skandia, and the Handelsbanken sphere (a traditional Swedish "control owner") had both stepped away from Skandia by 2004 (*Table 9*), leaving the company in the control of the Swedish "institutional

banes-Oxley Act 2003. Skandia led to the introduction of a Swedish corporate governance code (2004).

investor community" and their foreign equivalents. Thus, Skandia's shareholder structure remained both dispersed and changing, which complicated the governance work both from the perspective of the nomination committee, made up of representatives of the largest owners, and the board of directors. Skandia had emerged as the perfect takeover candidate. As a result interested parties and their advisors circled Skandia looking for a bargain.

7.2.2 Process leading to the bid

Skandia's recovery was to be led by new CEO Hans-Erik Andersson, who came from the insurance industry and had a background in Skandia. Andersson took office on 1 January 2004. Because of previous scandals, the board and the chairman that had appointed him resigned, and the new CEO, who hade been falsely associated in the media with the earlier scandals, was left with a rather weak position (Kallifatides, Nachemson-Ekwall & Sjöstrand, 2010).

With this great uncertainty, a set of Swedish institutional investors making up the nomination committee[89], presented a "board of trust" to the annual general meeting in April 2004. Into this extraordinary situation, renowned Swedish industrialist Bernt Magnusson was appointed chairman of Skandia. Magnusson had a long track record with corporate restructuring. The four Swedish institutional investors that made up the nomination committee had formulated the idea that chairman and vice-chairman Björn Björnsson would work closely with the CEO and "support" him. For this, they were to be given additional compensation, to be phased out when the workload diminished. Andersson was not to be a member of the board, in line with the post-millennium Swedish govern-

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[89] In March 2004 these were SEB Funds (4.2 per cent), Swedbank Robur (3.9 per cent) and AP2 (2.5 per cent) and Handelsbanken (2.4 per cent). In November 2004 they were SEB Funds (5.7 per cent), AP2, Robur and Nordea. Together five Swedish institutional investors controlled 22 per cent of the shares. In November 2003 they owned six per cent.

ance model, creating a clear separation of power between the board and management.

Thus, by April 2004 Skandia was set for a turnaround. This was not to be a simple matter however. Skandia shares were trading at around 30 SEK, giving a corporate value of SEK 30 billion (GBP 23 billion). In the eyes of many this still reflected a share price pressed by reputational damage, trading at a discount to both Skandia's break-up value and long-term profit prospects. There was a new board and new management in place. The most important issue to address appeared to be the UK business, with the subsidiary Skandia Life UK. In 2004, the UK business made up half of Skandia. Skandia was performing badly and the Skandia Life UK was seemingly in worse shape than the rest of the company. However, the UK management did not want to cooperate. It became clear to everyone inside the company, the board of directors, and many outsiders as well, that this situation would have to be tackled to make Skandia reach its potential.

Complex relationships characterized the new Skandia leadership in 2004, both between the CEO and the chairman and deputy chairman and between the chairman and deputy chairman and the other directors. The ordinary directors had difficulty finding their role and informally something of a two-tier board emerged. The new chairman and the deputy chairman received a board mandate to engage investment bank Morgan Stanley to review Skandia's strategic position. One of the suggestions that came up was that the UK subsidiary be sold off. At a board meeting in August 2004 some of the directors opposed this idea, arguing instead for a plan to let the CEO and management focus on internal restructuring and a cost-savings program, an argument that gained general board support. As a result the investment bank's work with Skandia came to an end.[90]

However, already later in the autumn of 2004 chairman Magnusson talked to the four members of the nomination committee, four Swedish institutional investors that together represented around 15 per cent of

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[90] Morgan Stanley had a normal "retainer agreement", which was to be terminated at the end of 2004. MS did not do any work in the autumn of 2004.

Skandia's share capital. The Skandia chairman asked for and received their support for further strategic analysis by the investment bank Morgan Stanley. The majority of the directors on the Skandia board remained uninformed about this.

Early December chairman Magnusson gave an interview in Sweden's leading daily newspaper (Dagens Nyheter, Gripenberg & Lucas, 2004, 2 December). The title of the piece was "Skandia's chairman open to sale". Investment bankers, legal advisory firms and other potentially interested parties acted instantly to position themselves for an expected structural deal. The rest of the Skandia board were not informed about the chairman's stance in advance of the media report. On December 14, activist investment fund Cevian and its CEO Christer Gardell flagged for 3.4 per cent of the shares in Skandia. This was communicated in public as a means of generating interest, which it certainly did as well-known US activist investor Carl Icahn was a co-investor in the Cevian fund. Two Swedish national pension funds were also found among the investors, AP1 and AP2. A few weeks later, Gardell was drafted into the shareholders' nomination committee preparing for suggesting directors ahead the upcoming AGM. In the winter of 2005 Gardell marketed Cevian's own valuation of Skandia, in which the insurance company was said to be worth SEK 60–70 billion, rather than the SEK 30 billion it was then trading for. Gardell gained support from many investors, including two Icelandic investment banks.[91]

One of the actors that contacted the chairman of Skandia early in December 2004 was South African/British listed financial conglomerate Old Mutual (see *Table 10* for the competitive landscape). OM had legitimate reasons for looking at Skandia. At the time OM wished to diversify its portfolio offering by acquiring a fast-growing savings company, reduce its own exposure to the South African home market and become large enough to be included in the investment indices that large London-based institutional investors followed. In this context Skandia was somehow the perfect target with its focused business offering

[91] These were Burdaras and Kaupthing, both of which featured prominetly in the Icelandic banking crisis in 2008.

and open shareholder structure. At the time OM was trading at a heavy discount to industrial peers and had a strong cash position, with institutional investors pressing for a dividend pay out. OM CEO Jim Sutcliffe was highly respected.

Table 10. The competitive landscape

European insurance companies 2004	AuM Billion £
Allianz	770
AXA	630
ING	370
Aviva	300
Generali	240
AEGON	220
Prudential	200
L&G	180
Old Mutual	160
Skandia	50

Kallifatides et al. (2010)

In late December 2004 Skandia's chairman and deputy chairman signed an agreement with Skandia's investment bank Morgan Stanley to prolong its mandate to pursue a strategic review, this time dealing with possible interested parties. The rest of the board was informed about the new agreement with the investment bank at a board meeting in January 2005. This was clearly upsetting to the majority of the directors and heated discussions led to the decision that Morgan Stanley's (MS) work should be monitored closely to ensure that MS acted passively, as the directors concluded that MS would be keen to find suitors. The chairman and deputy chairman agreed to this arrangement. At this time MS also presented different calculations on the potential value of Skandia, varying between a fair trading value of 35-38 SEK per share and a possible value above 50 SEK if a bid from an industrial party emerged. In the winter of 2005, MS' team worked actively to find parties interested in acquiring Skandia, or parts of it. During late winter and spring the CEO, Andersson, tried in various ways to make directors attentive to MS's activities, which appeared inconsistent with the board's decision.

In early 2005 the Skandia nomination committee was made up of four Swedish institutional investors, two retail funds from bank groups, Swedbank Robur and SEB, one national pension fund AP2 and Cevian, the activist hedge fund. Together these funds were in control of less than 15 per cent of Skandia's capital. Gardell was nominated for a board seat and he received additional support from Skandia's then largest shareholder, the US-UK based retail fund Fidelity (which had abstained from participation in the nomination committee) and the group of Icelandic investors. Gardell travelled to London and met Skandia's UK management, only to come back supporting chairman Magnusson's view that the subsidiary or the whole of Skandia should be sold. Gardell also held private meetings with Old Mutual's CEO.

7.2.3 The Actual bid

In May 2005, an employee at Cevian leaked to the stock market that OM was offering to buy the whole of Skandia with a mix of cash and shares at a price of SEK 45-48 billion.[92] This pushed the Skandia share from 33 SEK to 41.6 SEK, a twenty per cent rise. The idea of mixing cash and shares came from OM's investment bank Merrill Lynch, which had ample experience of cross-border European bids. The mix was

[92] The employee was later charged for insider trading but was freed in what has otherwise been known as the largest insider scandal experienced in Sweden. The person was fired from Cevian as he had acted in conflict with his employment contract. He was later found not guilty in court for insider trading but convicted for tax evasion.

meant to ensure that incumbent shareholders in the target company could sell off shares to groups of international arbitrage investors ahead of the closure of the bid.

OM conditioned the bid on both a positive board recommendation and the opportunity to perform a due diligence on Skandia, i.e. access its internal books and records. Several Skandia directors opposed this. However, MS advisors described it as standard practice. Gardell argued that refusing OM the opportunity to carry out a due diligence would expose the board to legal action. In the end, the board agreed to accord OM and other interested parties the right to pursue a due diligence.

During the summer MS set up an "auction process", in which possible suitors were asked to come up with offers based on public information. MS' team tried to put together a "theoretical consortia" with interests in different parts of Skandia but with the ability to acquire Skandia in its entirety and pursue a break-up later. However, OM seemed to be the only one interested in the whole of the company and also offered to pay the highest price. At the same time the bidding process dragged on and frustration grew within Skandia management and among sceptical directors. In July both Björn Lind, head of SEB retail funds and chairman of Skandia's nomination committee, and Gardell contacted Skandia's largest shareholder, the asset manager Fidelity International in London, for support in favour of a deal. Fidelity consequently called chairman Magnusson, who suggested that Fidelity write a letter to the board. Magnusson later read the letter to the board. The majority of the directors, however, remained sceptical. Together with deputy chairman Björnsson and director Gardell, chairman Magnusson made up a minority on the board clearly in favour of a deal.

In the middle of August 2005, OM and its advisors offered the Skandia board SEK 42 billion, which was lower than previous expectations. The reaction from the directors was rather cold, including the reactions from both the chairman and deputy chairman. Advisors on both sides believed that the deal was off. Andersson had by that time internal board support from the majority of the directors to continue with the work on a stand-alone strategy. At the time the profit prospects for the Skandia group seemed to be good. Among the more sceptical board members, director Lennart Jeansson, a respected Swedish industrialist, took a leading role.

However, the chairman and deputy chairman, alongside director Gardell, changed their mind in favour of the OM bid. Thus, in late August it was suddenly clear that the board would not be able to unite in support of a bid from OM. This was a complication as OM had conditioned its bid on friendly support from the Skandia board (which was not consistent with the Swedish Takeover Rules, which stipulate that a final proposal ought to be presented for shareholders to decide for themselves). The Skandia board, being split and unable to recommend the bid, instead informed Skandia's largest (institutional) shareholders about the dilemma. A group of around ten investors were invited twice to investment bank MS' premises in Stockholm to receive information, take part in heated discussions and offer recommendations to the board. All this was leaked to the media (for a detailed description see Kallifatides, Nachemson-Ekwall & Sjöstrand, 2010).

The Skandia directors' compromise was to recommend OM that it put its 42 SEK combined share-and-cash offer to the public without having received a prior board recommendation. Hence, in the beginning of September 2005, OM presented its offer, including letters of intent to sell from 15 per cent of Skandia's shareholders ("soft irrevocable").[93] The media was filled with reports on the merits for and against the proposed deal.

7.2.4 Hostile bid

In early October, the board took a negative stance on the bid in public. The majority of the directors, five whom were nominated by the AGM and an additional three representing the Skandia employees, argued against the bid on grounds of both price and strategic gains for Skandia as a stand-alone company. There were serious questions concerning the possibility to realize synergies between Old Mutual and Skandia savings

[93] These "irrevocables" were signed by the national pension fund AP2, the Icelandic Kaupthing, the activist Cevian and the SEB funds. AP2 later changed its position.

and pensions offerings. There were questions concerning Old Mutual's claim that it could contribute to Skandia's expansion, as Skandia at the time was cash flow positive and thus able to self-finance investments. Two directors presented worries concerning the future of Stockholm as financial center if Skandia was to be run from London (or South Africa). The chairman, deputy chairman and director Gardell were in favour of the bid. At that point the chairman, Magnusson, stepped down to be replaced by Jeansson. In late October and November the CEO, Andersson, embarked on a PR and defensive campaign in Stockholm and London, now aided by investment bank Goldman Sachs. By then, the Skandia board had decommissioned Morgan Stanley. Skandia and Goldman Sachs also prepared a defence document with detailed projections on growth and profit prospects.

In the late autumn, it turned out that there had been a radical shift of shareholdings in Skandia between 13 May 2005, when OM's intentions were first leaked and when the offer was formally rejected by the Skandia board on September 21 (*Table 11*). When Old Mutual had publicly presented its bid in early September, the board had been rather confident of having the support of at least ten per cent of the shareholders, a "controlling minority" (accorded various privileges in Swedish corporate law). Among early supporters were two national pension funds, AP4 and AP2 (the latter having made a surprising shift in its stance). The Swedish Shareholders Association gathered proxy votes from small shareholders equivalent to four per cent of the capital. Representatives from the Social Democratic government expressed public displeasure with Skandia being sold to a foreign entity but abstained from active involvement, partly from unwillingness to risk its good relationship with South Africa and partly because it did not want to be criticized for political involvement in the investments of the national pensions funds, the AP funds.

Table 11. Skandia's ownership structure

Shareholders	March 2004 (%)
SEB Funds	4.2
Swedbank Robur	3.9
AP2	2.5
SHB	2.4
Singapore	1.7
Alecta	1.4
Nordea Funds	1.3
AP4	1.1
AP1	1.1
Fidelity Funds	0.8
10 Largest	20.4
Market value	30 Billion SEK

Shareholder	November 2005 (%)	Stand on OM
Fidelity Funds	9	Yes
CSFB	5.4	Yes
Paulson & Co	5.1	Yes
Noonday	4.9	Yes
AP2	3.5	No
Cevian Capital	3.4	Yes
Swedbank Robur	2.4	No
SHB Funds	2.1	No
Nordea Funds	2.0	No
Straumar-Burdaras	1.6	Yes
Sw Shareholders proxies	3.8	No
Third Avenue	0.9	No

SIS Ägarservice (2004–5)

Instead Swedish institutional investors (which as expected had little interest in exchanging Skandia shares for OM shares) gradually sold off shares, choosing not to wait for the Skandia board to state its opinion on the bid, but selling instead on the basis of the short-term share rise relative to other financial stocks and portfolio allocation decisions. The buyers were foreign investors and mostly different kinds of short-term hedge funds and arbitrage investors. Among these were New York-based Paulson and London-based Noonday. The fact that going forward OM would be included in a large financial index helped increase interest for the OM stock among arbitrage investors, thus leading to a short-term rise in stock price.

After an uncertain start, OM's fortunes changed for the better in November, partly because of a rally on emerging markets that raised the OM stock to new heights, carrying the Skandia stock with it. By November 2005, it was also evident that the growing presence of an international group of hedge-fund investors had become a major obstacle for those who opposed the bid. The new nomination committee set up in the middle of November comprised of three fund managers in favour of the Old Mutual bid (Paulson, Fidelity and Cevian) and two investors opposing the bid (a representative from AP2 and AP4 and one from the Shareholders Association). OM then stated it would waive the 90 percent threshold and go through with its offer having secured little more than 60 per cent of the shares. At the same time the Skandia defence document backfired as the document stating that Skandia's stand-alone plan would enhance shareholder value worked to assure hedge funds that OM was likely to make a good deal by buying Skandia despite its hostile approach. It also emerged that the position of the OM CEO, Sutcliffe, was much stronger than CEO Andersson's in Skandia. When the Skandia chairman Jeansson had turned to the chairman of OM with a request to withdraw the bid, the response was that the OM chairman was in no position to make such a decision given the standing of the CEO.

Skandia chairman Jeansson continued working with a small group of resistant incumbent Skandia investors to stop the bid until the end of January 2006. They failed; among the reasons were an out-dated Swedish insurance law that did not address minority shareholder rights applicable to other Swedish companies; aggressive trading by arbitrage funds ready to keep buying shares from incumbent Skandia shareholders; and regulation of retail funds preventing them from investing in delisted entities. The Skandia board and Swedish investors also spent time searching for a white knight but no one emerged. Among those targeted for investing in Skandia was Skandia Liv, the mutual that was owned by Skandia through a hybrid legal construction.[94]

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[94] In December 2011 Skandia Liv acquired Skandia's Nordic business operation from Old Mutual.

To have the bid finally accepted by almost all shareholders OM took advantage of a legal device called the *Forced Merger Rule*. At the time of the Skandia-bid a bidder, following an acquisition of 66.7 per cent of the shares, could reserve the right to take actions in order to initiate the implementation of a statutory merger between the bidder and the target. This was due to unintended consequences in a change in the Swedish Companies Act around the millennium.[95] In the Skandia bid it was used by OM to circumvent the 90 per cent minority-protection rule in the Companies Act. Following the OM hostile takeover of Skandia, battles for corporate control on the SSE would be waged for 66 per cent ownership rather than 90 per cent, as had been the case under the Companies Act. It would certainly be less expensive to bid for only 66 per cent of the Skandia shares rather than 90 per cent. By March 2006, OM was in control of Skandia. As the value of the OM share had increased, the last shares were acquired for 52 SEK. The Skandia CEO Andersson left and was replaced by an Old Mutual executive.

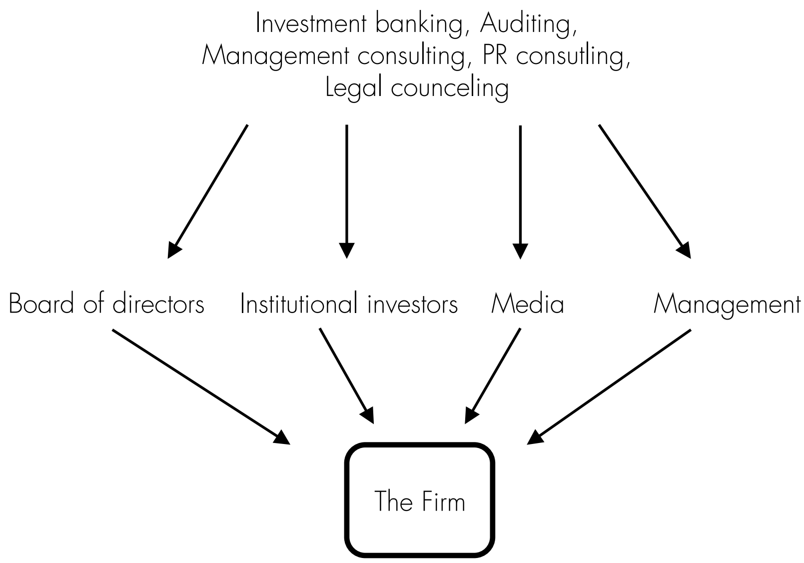
7.3 Analysis of the Skandia study

The OM-Skandia study gives a picture of actors and forces involved in a cross-border hostile bid during financial capitalism that differ greatly from those at work on an allegedly efficient market for corporate control (Manne, 1965). Rather the outcome can be described as reflecting an "informal hierarchy of governance" *(Figure 11).* The OM-Skandia study

[95] The Swedish Companies Act allows the offeror to acquire minority shareholdings on a compulsory basis if it owns 90 per cent of the shares and voting rights in the target. The 90 per cent rule also implies that minority shareholders have the right to be bought up. An arbitrator is consulted to settle the agreement on price between disputing parties. This cornerstone of Swedish minority protection was set aside after the Companies Act was revised around the millennium when Sweden adopted a force merger rule in line with the implementation of new EU regulation (Ministry of Justice, Skog, proposal 2006:07:70).

reveals three parallel contingencies that can be said to impact a cross-border hostile-takeover process in the era of financial capitalism: the Swedish model of corporate governance, short-termism among institutional investors and regulatory and moral arbitrage. This is outlined in more detail below.

Figure 11. Actors and Forces (the informal hierarchy of governance)



After Kallifatides et al (2010)

7.3.1 Swedish model of corporate governance

In Skandia the combination of a dispersed shareholder structure and a board of directors controlled by (short-term) institutional investors made it hard for Skandia's board to focus on the work of long-term value creation. The board's mandate from shareholders was vague. The board also lacked the means to protect Skandia from a bidding party. The effect was that the board split into three groups. At the time of the Old Mutual-hostile bid, in September 2005, there were three conflicting positions represented in the Skandia board:

- Short-term shareholder value: the argument being that an offer clearly exceeding current market value was on the table and should therefore be accepted.
- Long-term shareholder value: the argument being that the market had yet to realize the potential of the company, but would do so in time and thus create more value to shareholders in the future than the bid on the table.
- Stakeholder value: the argument being that from the point of view of certain stakeholders there are important externalities involved in controlling a company, and the price to be paid for these externalities is foregoing, at least, this particular opportunity to realize a profit.

As the struggle over corporate control moved on, the long-term value-creating position and the stakeholder-value position coincided in practice. This evolution can be summed up as: “An independent Skandia is good for the financial market in Stockholm and hence for a large actor such as Skandia.” However, it was the short-term position that won in the end, which takes us to the second theme.

7.3.2 Short-termism among institutional investors

At the time of the Old Mutual bid Skandia appeared to house a large group of institutional investor-owners that followed a financial rationale and sold off shares for index-tracking reasons rather than operational reasons. When the Skandia board, in accordance with the Swedish takeover regulations, publicly expressed its negative position towards the bid a large number of incumbent (institutional) shareholders had already sold their shares to different arbitrage investors and hedge funds that were ready to accept the OM bid. In addition, the structure of the Old Mutual bid, with a combination of shares and cash, was especially designed by the bidder's investment bank to encourage this type of sell off. The defence document worked to support arbitrage investors in buying Skandia shares, thus driving the share price short term and further enhancing the sell decision by incumbent (short-term) institutional investors. For Skandia, as a Swedish public company with a dispersed ownership structure and a board prevented from using defence tactics to fend off a hostile suitor (other than marketing), a parallel portfolio allocation and short-term rationale of institutional investors, here especially the AP funds and the Swedish retail funds, was detrimental to its survival as an independent entity.

7.3.3 Regulatory and moral arbitrage

National rules and regulations enable arbitrage between different systems of corporate governance. In the OM-Skandia process the use of the due diligence technique was important. The practise emanates from the US and has thus evolved to work in a US context. The Skandia directors had little confidence or experience with the dd-process, and the management appeared to be occupied with the dd-process for three months. In the end this work made the bid's success inevitable, as it had both put Skandia "in play", and resulted in a lower bid than the board anticipated at the start of the dd-process.

Other examples were the work of the investment bank Morgan Stanley as both the preparer of a fairness opinion (which was never published) and receiver of a success fee. In a Swedish context, where the board is legally obliged to take a passive stance during a bid, this way of paying advisors complicates the role of the investment bank vis-à-vis the board. It is here in the investment bank's absolute interest to have a bid presented as it earns money from the actual transaction. As such the recommendation and activities from an investment bank might not prioritize the business rationale of the target company at all.

Furthermore, the mandates given the boards of Old Mutual and Skandia differed. OM's directors (following UK governance) both acted more independently of its shareholders and allocated more power to the CEO than its counterpart at Skandia. Therefore the playing field shared by the directors of the bidding board and the directors of the target board was fundamentally uneven.

There were also strict legal conditions in the Swedish Companies Act related to the protection of minority shareholder rights. To have the bid accepted OM took advantage of the forced merger rule, which made index-tracking institutional investors sell their stocks as they were restricted from investing in a delisted entity with an illiquid share.[96]

The OM-Skandia process also revealed what can be described as "moral" arbitrage in the sense that some actors did what other considered, for some reason or another, ethically inappropriate. Examples included the Skandia chairman's contacts with the nomination committee concerning support for an overview of Skandia's position in the autumn of 2004 without the prior consent of the board, the chairman's unexpected newspaper interview that put Skandia "in play", and the chairman and deputy chairman's talks with the investment bank MS concerning a possible deal, again without previous discussion with the rest of the Skandia board. Another example of "moral arbitrage" was the action taken by the employee at Cevian, who in May 2005 leaked that Old Mutual was offering to buy the whole of Skandia. Again, during the summer of 2005 the chairman of the nomination committee and Cevian's Gardell, then a director of Skandia, both contacted Skandia's largest shareholder, Fidelity International in London, for support in favour of a deal, and Fidelity consequently called Skandia's chairman, who suggested that Fidelity write a letter to the board. The other directors were not informed about this chain-initiative. Yet another issue, closer to some sort of indirect moral arbitrage was the usage of the words "friendly" and "hostile" bid. When OM first approached Skandia it made clear that it

[96] This ended in 2007, when the Swedish Companies Act was revised in order to terminate actions that were perceived by many market actors as misuse of the Forced Merger Rule in listed companies.

was only interested in making a friendly bid that received board support. This was an important condition for the Skandia board's decision to allow OM to conduct a due diligence. However, when it later became clear that the Skandia board was split, and the chairman even resigned, the OM CEO received its board's support for continuing with an outright hostile bid.

7.4 The Capio case[97]

In the joint hostile takeover of the health-service provider Capio by the private equity firms Apax and Nordic Capital through the company Opica in 2006, there is a follow-up to Old-Mutual's cross-border hostile bid on Skandia.

Just like Skandia, the target company Capio had a dispersed shareholder structure and many of the institutional investors present in Capio were previous investors in Skandia. The case can be seen as a cross-border fight because the bidding parties were foreign incorporated private equity funds, one of which, the lead actor Apax, had foreign management and ownership (French and British). The bidders also operated with a different governance model, attuned to the financial rationale of the private equity industry (for a description of the PE industry see Kaplan and Strömberg, 2008).

7.4.1 Background

The predecessor of Capio, Bure Health Care, started as a subsidiary to the Swedish investment company Bure.[98] It was founded in 1994

[97] This is a summary of my empirical case study "The Hostile Bid on Capio 2006" (Nachemson-Ekwall, 2012b, unpublished manuscript). The case is built on a combination of open media sources and a handful of interviews conducted by myself during the autumn of 2010. The complete case study includes an extended list of references.
[98] Bure Förvaltnings AB was formed on 23 November 1993 in Gothenburg with a stock portfolio and cash at a value of just under SEK 2.2 billion from the *Wage Earn-*

through the acquisition of Nove Medical, a provider of laboratory services. That year Bure Health Care also bought Lundby Sjukhus in Gothenburg, in what was the first sale of a municipal hospital to a publically listed company on the Stockholm Stock exchange. Thus Capio became an early private actor in the liberalized Swedish health-care service sector. Two people were behind the Capio expansion, Bure's CEO Roger Holtback and the head of Bure Health Care Per Båtelson.[99]

By the year 2000 the health-care service provider had grown to a turnover of SEK three billion (GBP 220 million). Its name was changed to Capio, and the group demerged from Bure Equity in October 2000 to be listed on the SSE. Båtelson continued as CEO and Bure's CEO Holtback was appointed chairman, a position he kept even after leaving Bure in early 2001.

At the time of the listing in 2000 Capio's ownership structure reflected the shareholder structure of Bure, which was spread among a broad group of Swedish and foreign institutional investors *(Table 12)*. There was only one series of shares, which meant that Capio, like Bure, deviated from the traditional governance structure with a dominating shareholder exercising its control through A and B shares, with the A share given multiple voting rights. The abandonment of the multiple voting structures reflected the demand of investment banks and institutional investors. It also reflected expectations that the EU in its work with the directive on takeover regulations would stop multiple voting stocks. At the time of the listing in October 2000 the dominant shareholder in Capio (and Bure) was the Sixth AP fund (AP6), which controlled 14.9 per cent of votes and capital.[100] Following the AP-fund were nine institutional investors all of which were Swedish but one, Orkla, a Norwegian retail

ers' Investment Funds. These were a rest from residual capital from an attempt by the Social Democratic government to socialize ownership of the Swedish industry in the early 1980s.

[99] Per Båtelson had a background from the medical industry. Roger Holtback was previously a high-profile director of Volvo Cars, then a subsidiary of Volvo AB, and after that a director of Skandinaviska Enskilda Banken in Gothenburg, later SEB.

[100] Shortly after Capio was listed AP6 increased its stake to 17.4 per cent, SIS December 2000.

fund. However, in all 34 per cent of the capital was controlled by foreign investors, a sharp increase from 21 per cent a year before.[101]

Table 12. Capio's ownership structure 2000

Shareholders	December 2000 (%)
AP6	14.9
Orkla AS	7.3
AMF Pension	4.5
Skandia	4.3
SHB Funds	4.0
SEB Funds	3.4
SPP	2.8
KP Pens and Ins	2.1
Folksam	2.1
Skandia Funds	1.2
10 Largest	46.6
Market value	SEK 3 Billion

SIS Ägarservice (2000)

The listing of Capio was a success. After three months, at the end of 2000 Capio's market capitalization had increased by 40 per cent to SEK 4.1 billion (GBP 360 million). During the same three-month period the SSE fell by 10 per cent. In the spring of 2001 Capio made a rights issue of close to SEK one billion (GBP 87 million) to institutional investors to

[101] Bure Equity's refocus on TIME appealed to foreign institutional investors. Sweden was considered a "hot spot" for IT around the millennium.

finance expansion through acquisition. Investment bank Deutsche Bank acted as financial advisor and was to have a close relationship to Capio during the following years. Foreign interest in Capio increased and by the end of 2001 foreign investors controlled 58 per cent of the shares of Capio.

By 2005 Capio had grown into one of the leading healthcare service providers in Europe with operations in a dozen countries. The Capio Group had annual net revenues of approximately SEK 13 billion (GBP 1 billion), with some 15,000 employees. The market capitalization had tripled in less than six years. Capio was described in media as the "Swedish healthcare service miracle" (Affärsvärlden, Isaksson, 2006, 15 January).

In the summer of 2005 CEO Båtelson informed chairman Holtback that he wished to step down, and was replaced as CEO by Ulf Mattson. Holtback remained chairman. In February 2006 another rights issue of SEK two billion was announced with the aim of increasing growth and acquisitions. Deutsche Bank and Nordea acted as financial advisors. CEO Mattson was quoted in the weekly Affärsvärlden as saying that this was still only the beginning (*Ibid.*). Capio appeared to have good momentum. The Q1 report presented on April 25, 2006 came in strong and the share rose by 3.5 per cent to SEK 159.

However, during the weeks following the Q1-report, Capio ran into trouble. The rights issue planned for mid May came at a time with much uncertainty on the stock market, which pressed the Capio share.[102] There also appeared to be problems with the UK business and the Swedish business was troubled by changes in the management team. Capio's foreign investors started a massive sell out, reducing foreign shareholding from 55 per cent of the shares in April to 45 per cent a month later. At the end of May Capio stock was trading at SEK 132, and by June it had fallen back to 120. Media wrote that Capio was inexpensive, which together with the open shareholder structure made it a perfect takeover candidate (Dagens Industri, Wäingelin, 2006, 1 July).

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[102] Sudden fear of a world economic slowdown led to a drop in global equities. On 22 May SSE fell by 5.3 per cent, the largest one-day drop since 11 September 2001. That meant that the whole rise of 12 per cent since the beginning of 2001 was erased.

In June 2006 ten institutional investors, including two AP funds and Norwegian Orkla, controlled one third of the company *(Table 13)*. Of these Orkla, AP2 and AP4 made up the nomination committee, together with Capio chairman Holtback. When the Q2 report was presented on 26 July financial analysts and investors were again surprised by weak results. Capio shares fell to SEK 107, a 16 per cent drop in the share price. However, Capio's growth strategy continued and two acquisitions were announced before the end of August. Capio also communicated a plan to buy three or four new companies within the next 18-24 month.

Table 13. Capio's ownership structure 2006

Shareholders	June 2006 (%)
Foreign Investors	44
of which Orkla	5.2
AP2	6.3
AP4	5.3
Swedbank Robur	4.0
AFA Ins and Pens	3.7
SEB Funds	2.3
SHB Funds	2.3
Folksam Insurance	1.6
AMF	1.5
Market value	SEK 11.3 Billion

Shareholders	October 2006 (%)
Foreign Investors	59
of which Orkla	5.1
AP2	6.3
AP4	5.3
AFA Ins and Pens	5.3
Swedbank Robur	3.7
SEB Funds	2.4
Catella Funds	2.1
Carnegie Investments	2.0
SHB Life and Funds	1.6
Market value	SEK 17 Billion

SIS Ägarservice (2006)

On September 1, Opica AB, owned by the private equity funds Apax Partners Worldwide, Nordic Capital Fund VI and Apax France, bid SEK 15.8 billion (GBP 1.15 billion) for Capio, equivalent to SEK 153 a share. The offer gave a 25 per cent premium on the previous trading price and a premium of 35 per cent on the average closing price of SEK 113.35 for the Capio share during the last 20 trading days prior to announcement of the bid.

7.4.2 Process leading to the bid

Capio CEO Båtelson had over the years faced different bid offers, but he had been able to talk both the management team and the Capio board into turning down any offers in favour of his own vision of Capio as an endless growth story.

A first offer had actually come from Nordic Capital at the time of the IPO in 2000. The Nordic Capital team lacked experience from the industry and needed the support of the management team. In 2002 Nordic Capital CEO Robert Andréen again presented a buy-out case to the Capio board, which again turned down an offer. But the management team weakened when Båtelson left and was replaced by a less well-known CEO, Mattson.

In 2005 PE fund Apax began to look more closely at Capio. Apax had global experience from the healthcare and service industries. In early 2006 Apax representative Lars Johansson approached previous Capio CEO Båtelson and invited him to become lead manager of an Apax bid for Capio. The Capio board and new CEO Mattson became aware of Apax's and Båtelson's interest in Capio in the winter of 2006. All along Apax had abstained from making direct contact with Capio. However, other PE funds did contact Capio. These included Nordic Capital, CVC and PAI Partners, the PE fund controlled by the French bank Paribas. In the spring Båtelson suggested that Apax join forces with Nordic Capital, to bring a trustworthy Swedish partner into the deal.

In July the Capio board enrolled investment bank Morgan Stanley as an advisor in the event that a bid was presented. By the end of August the board was more or less just waiting for a bid. Three indicative bids came to the Capio board from Apax/Nordic Capital, Cinven and PAI Partners. Apax/Nordic Capital announced its offer in public on September 1.

When the bid was made public on September 1 Capio's shares rose by SEK 45.5 and closed at SEK 168 a share, indicating market expectations of a bid rise, either from Apax/Nordic Capital or from competing private equity firms. There were also indications that the bid had leaked to stock market actors. Two weeks before the bid announcement turnover in Capio shares had increased four fold compared to trading volumes during the year (News agency Direkt, 2006, 1 September). The share price also rose by 10–15 per cent.

These market movements had speeded up the takeover plans, according to statements by representatives of Apax and Nordic Capital during a press conference presenting the bid for the media and analysts. The representatives of Apax Partners and Nordic Capital had been openly pleased – and confident – during the press conference.

7.4.3 Hostile bid

The Capio board immediately rejected the offer. In a public statement the board wrote that the bid did not adequately reflect the value of Capio shares, given Capio's attractive growth prospects and business fundamentals. Now investment bank MS was to work with the preparation of a defence document from the Capio board. MS was also to prepare both a fairness opinion and an auction process during which Capio would open its books for a due diligence process. MS was to receive a success fee related to a final bid value.

The board's stance was not straightforward. Due to conflicts of interest, Capio's chairman Holtback did not participate. Holtback was also chairman of the bidding PE firm Nordic Capital's deal-review committee. Instead director Krister Hertzen would represent Capio in matters relating to the bid. The Swedish Shareholders' Association, Aktiespararna, questioned Holtback's conflicting roles and media wrote critical articles (e.g. Göteborgs-Posten, Lövgren, 2006, 2 September). Holtback said that he had informed Capio's board of Nordic Capital's plans in July and that a week before the bid had been made public he informed the board that Nordic Capital finally had decided to make a bid and thus he would abstain from continued board work in Capio, due to conflicts of interest.

In a statement the Shareholders' Association criticized the bidding parties for having misused the fall in Capio's stock value following the second quarter report. It also argued that advisors involved had conflicts of interests. For example, the offer was not subject to any conditions concerning the availability of financing. Despite the fact that Opica had not pursued a due diligence it had received commitments for credit facilities for the debt financing from the Royal Bank of Scotland (RBS) and from Barclays Bank PLC (the "Banks"). Opica also retained Deutsche Bank as a financial advisor in connection with the offer. That was the same Deutsche Bank that had administered Capio's rights issue in May. This meant that a Deutsche Bank team during the spring had had full insight into Capio's financial matters, knowledge that RBS now appeared to be able to rely on. So the bidding parties appeared to be ably to rely on at least two clear Capio connections – Deutsche Bank and Holtback. A delicate issue was also the role of former CEO Båtelson, now acting as advisor to the Apax group.

Possible conflicts of interest also applied to a number of Capio's shareholders. AP2 was the largest shareholder in Capio, with 6.3 per cent of the shares, and it had also SEK 500 million committed to Nordica Capital Fund VI, one of the funds behind the bid on Capio. Capio's fifth largest shareholder, AFA Insurance with 3.7 per cent of the shares had also committed money to the Apax Europe VI fund.

The bid on Capio had spurred reactions all over Europe. Industrial competitors in the health service provider sector rose on speculations of similar PE bids. On Monday, September 5, Capio share peaked at SEK 172. That day Capio's Deputy chairman Hertzen said in the media that more bids were to be expected (News agency Direkt, 2006, 5 September).

By the second week of September foreign institutional investors had increased their holding of Capio shares from 45.8 per cent on the day before the bid, when SIS Ägarservice had published its latest ownership report, to 56.9 per cent a week later. AP2, AP4, and Orkla had not traded at all and were planning to act in concert going forward to be able to exercise pressure on Opica.[103] Lannebo Funds, Skandia Funds and First Nordic Funds no longer figured among the fifteen largest owners. The media named parties that might be preparing competing bids (e.g. Dagens Industri, 2006, 25 September).

One reason for Capio's potential was supposedly hidden value in Capio's hospitals. According to different analysts Capio's property portfolio might be valued SEK ten billion, indicating a cash takeout close of SEK three billion and a share value of around SEK 190. A PE bidder would also be able to work with a higher debt ratio and as a result deploy less capital. The media wrote that Capio's internal five-year plan revealed a potential to increase internal corporate efficiency, which could increase the profit margin from 6.8 per cent at the time to a suggested nine per cent within a few years (Dagens Industri, Nachemson-Ekwall, 2006, 5 September).

Two weeks after the bid had been announced, on Friday 15 September, the Shareholders' Association recommended that private investors turn down the Apax/Nordic Capital bid. The Association claimed that Capio had an interesting market position and had excellent opportunities to finance its expansion through the stock market. According to the Association it was also ”unacceptable” that Opica in its prospectus threatened to delist Capio and pursue a ”forced merger” (for an explanation see below).

In a statement dated 19 September the Capio board of directors deemed the bid unacceptable. The Capio board instead worked on a defence document claiming that Capio had excellent growth prospects on a stand-alone basis and hoped to persuade incumbent institutional investors to remain long-term shareholders. However, many of them had already sold out, and yet others were uninterested in supporting a withdrawal of a bid that would result in a (short-term) fall in the share price. Instead, fighting for a higher bid by inviting other bidding parties

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[103] By acting together early in the process they had hoped to be able to deal with the bid on Capio better than they had done during the Old Mutual-Skandia battle a year earlier. This was not announced publicly because there are no obligations to do so in Sweden (see also in Sections 8.5.2 and 8.5.3).

or publishing a defence document with a positive outlook became the only possible action for the Capio board. On September 25 media reported that the Capio board had invited different PE funds to pursue a due diligence (Svenska Dagbladet, Braconier, 2006, 12 September).

For shareholders that wished to see a bid rise, or had hopes of a withdrawal, there was also a worry of strict legal questions related to the Forced Merger Rule. On the basis of this rule a bidding party could delist a company after having gained control of 66 per cent of the shares and as a consequence force most institutional investors to sell off their remaining shares. When Opica's bid was announced on 1 September, Nordic Capital had warned that delisting was one possible outcome. In a letter to the Swedish Securities Council (*Sw:* "Aktiemarknadsnämnden") the two national pension funds, AP2 and AP4, together controlling 11.6 per cent of the shares in Capio, questioned Opica's right to circumvent the 90 percent minority-protection rule in connection with the takeover rules. This was the same rule that had been decisive for OM's success in Skandia a year earlier (Ch. 7.2.4).

Towards the end of September the bid process pressed the Capio board. No competing bidder emerged, and Capio shares fell back. However, the turnover in the shares remained high, indicating that incumbent investors continued their sell off to arbitrage investors. On 2 October, Opica received clearance from the Swedish Securities Council to apply the Forced Merger Rule. Despite the fact that the Swedish parliament by now was working on legislation to put an end to the Forced Merger the Securities Council ruled that it was applicable to Capio since it was mentioned in the prospectus to shareholders.

On 5 October 2006, Opica AB finally decided to increase the offer price to SEK 167 in cash per share, an increase of 9 per cent compared to the original offer, and valuing Capio to nearly SEK 17 billion. This time the board of directors of Capio unanimously recommended that Capio shareholders accept the offer.

The Shareholders' Association joined the board in recommending the bid. However, the Association's representative Gunnar Ek was quoted in the press as saying that he was disappointed that the Stockholm

Stock Exchange would lose its last healthcare service provider (Dagens Industri, Palutko Macéus, 2006, 13 October).

7.5 Analysis of the Capio case

The Capio case features the same three parallel contingencies as in the cross-border hostile bid involving a Swedish actor that surfaced in the Skandia study. By way of review these are: the institutional investors, the Swedish governance model, and regulatory and moral arbitrage. They are outlined in what follows:

7.5.1 Institutional investors and the Swedish model

In the Opica-Capio deal, institutional investors followed the same financial rationale present in the Skandia deal. Governed by a strict financial rationale the majority of them sold off shares after the bid was presented for index tracking reasons rather than operational reasons. Emerging on the buy side were short-term investors such as event-driven hedge-funds ready to gamble on a possible sweetening of the bid. The Capio management and board had a business case and growth strategy in place so there was a possibility that the bid fight could resemble a Manne-style fight between competing management teams on a competitive market for control. In reality the fight was far from Manne-like as the takeover seemed to be more related to (opportunistic) financing by the Royal Bank of Scotland[104], combined with good support from related parties. In a situation with a sudden, and short-term, drop in the share price, there was no way Capio with its dispersed shareholder structure and Swedish governance regime could protect itself from a hostile bid. The drop in the share price during the summer enabled a bidder to make an offer attractive enough to entice institutional investors focused on quarterly, "short-term" performance to sell off for portfolio-allocation reasons. Re-

[104] RBS was one of the first large banks to crash in the financial crisis of 2008.

stricted by a board neutrality rule the directors could only present a defence document emphasising Capio's long-term growth prospects on a stand-alone basis, but that only to entice a higher bid and not with the aim of keeping Capio independent.

7.5.2 Regulatory and moral arbitrage

The Capio bid involved a legal complication related to the Swedish Companies Act and the protection of minority shareholders. To gain acceptance of the offer Opica took advantage of the "Forced Merger Rule", which had also played a part in the Skandia deal (AMN 2006:30; Nachemson-Ekwall, September 29, 2006, Dagens Industri). Legislation allowed an acquirer of 66.7 per cent of the shares to take actions in order to initiate an implementation of a statutory merger between the bidder and the target. Despite the fact that all actors on the Swedish market at the time agreed on the necessity for amending the rule, the Swedish self-regulatory body the Swedish Securities Council gave Opica clearance as they had correctly informed on the matter in the prospectus. As a result Opica was allowed to pursue an activity that distorted the minority protection rights of shareholders and put them in a position that made it impossible to abstain from accepting a bid offer.[105]

The question of moral arbitrage relates to the different positions taken by Capio chairman Holtback, the previous Capio CEO Båtelson and Capio's financial advisor, the investment bank Deutsche Bank. All three participated on multiple sides in the takeover process. Conflicts of interests have always been an integral part of the Swedish governance model, where blockholders and controlling shareholders participated actively on the board, and there is a tradition of close relationships between a company and specific banking groups. However, the Capio case appears to add some new dimensions to the problematic of conflicts of interests, emanating from new actors in financial capitalism. Holtback was both chairman of Capio and chairman of the bidding PE funds Nordic

[105] The practise was brought to an end with the introduction of a law to stop the activity 1 July 2007.

Capital's corporate review committee. Previous CEO Båtelson was enrolled by Apax to work on the buyout in early 2006, shortly after having terminated his employment with Capio, and it was he who suggested that Apax join forces with Nordic Capital to get a trustworthy Swedish partner in the deal. Apax's investment bank Deutsche Bank assisted Capio during the rights issue in May 2006. At the same time the Royal Bank of Scotland produced the financial package of the deal without a due diligence, indicating that it felt confident enough with the assurances presented by Deutsche Bank, Holtback and Båtelson.

Morgan Stanley worked with Capio on the defence while at the same time issuing both a fairness opinion and receiving a success fee if there was a bid-rise or competing bid. As such Capio's investment bank was geared towards both enhancing a bid and maximizing a price offer. Two of Capio's institutional investors, the national pension fund AP2 and collective pension fund AFA were co-investors in the bidding funds Nordic Capital and Apax, which meant that they had interests on both sides. AP2 also had a representative on Capio's nomination committee involved in enrolling directors to the Capio board.

7.6 The Scania case[106]

The primary focus here is on MAN's bid for Scania, made on 18 September 2006. However, to fully grasp the activities of the actors and processes involved it is necessary to examine events as early as 1997 and as late as 2012 as the fight for corporate control continues.[107] All in all, the

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[106] This empirical discussion is a summary of material found in my extended case study "Scania, the Market for Corporate Control and the Mandatory Bid Rule" (Nachemson-Ekwall, 2012c, unpublished manuscript). The study is based solely on written publicly available material. The research stops as of July 2011. The extended case study includes a complete list of references.

[107] Here the empirical research stops as of 9 November 2011 when VW controlled 55.9 per cent of votes and 53.7 per cent of capital in MAN and 89.2 per cent of votes and 62.6 per cent of capital in Scania.

case involved six corporate actors – Scania, Investor and Volvo in Sweden, and MAN, Porsche and Volkswagen in Germany, along with institutional investors, corporate advisors like investment banks and law firms. It also involved regulatory bodies in Germany and Sweden, the European Commission, a number of politicians and media.

In the Scania case the governance structure of the six corporate actors both diverged and evolved in different directions during the period covered. Four of the companies involved, Investor, Scania, VW and Porsche, had controlling shareholders. The control of Scania featured a typical Swedish pyramidal-control structure, with Investor being controlled by the Wallenberg family through the Wallenberg Foundation and empowered by A and B shares, with A shares granted multiple voting rights (Högfeldt, 2004). German Volkswagen remained during the greater part of the period protected by the Volkswagen Law, with a golden share in the control of the Federal State of Lower Saxony and with rights to block other shareholders from influence. At the turn of the millennium VW-CEO Ferdinand Piëch together with other German business groups, fought hard to stop the EU from outlawing the golden share, and in this work gained the support from German chancellor Gerhard Schröder who in a previous role of State Premier of Lower Saxony had served on the VW board.

The Scania case also addresses the German corporate control structure of financial institutions, "Deutschland AG", a system of stakeholder governance that had insulated German corporate life from the global market since World War II (for a description e.g. Financial Times, Milne, 2009, 14 August). However, at the turn of the millennium German industry felt pressure to adopt a more Anglo-American shareholder-friendly governance model resulting in the breaking up of the system of close-knit control. This left the MAN conglomerate a target for break-up. Porsche, with a stake in state-controlled Volkswagen, remained in the control of the Porsche family during the entire period. After certain infighting among relatives Dr Ferdinand Piëch, former VW CEO and chairman, in 2009 emerged on top with Volkswagen also merging with Porsche. Swedish Volvo on its side went from a dispersed shareholder structure and a failed and very hostile attempt to buy Scania (a deal that was blocked by the EU) to control by Renault, in which the French state has a stake. Some of the shares Volvo had bought in Scania from the Wallenbergs and Investor were subsequently sold to German Volkswagen.

7.6.1 Background

Consolidation of the global vehicle industry took off in the 1970s and in the following twenty years 25 suppliers were reduced to six or seven (*Table 14*). In the spring of 1998 German vehicle producer Daimler, with the Mercedes brand, merged with US-based Chrysler to create a global presence. The quest for economies of scale spurred activity among other actors. This made the MAN Group, with a conglomerate structure and financial institutions as owners, a target. The same held true for Volkswagen with well over 300 000 employees, questionable profitability and a depressed share price. Both companies felt the pressure of possible hostile takeovers. At the turn of the millennium the VW Law was under scrutiny by the EU. From a governance perspective, the VW board was in firm control of a coalition of VW management, the union IG Metal and Dr Piëch, acting as CEO of VW and later as chairman. At the time Swedish heavy-vehicle producer Scania with its CEO Leif Östling remained an independent niche player, preferring to rely on alliances to gain economies of scale in production. Through the years Scania managed to maintain profitability above its peer group. Scania was partly owned by Investor, the listed investment company controlled by the Wallenberg sphere. In 1996 Scania was relisted at the SSE. Investor remained as the largest owner with 45 per cent of capital and votes.

However, after the IPO Scania's stock price fell and new shareholders were critical. At the time Investor's portfolio was realigned to reflect the popularity of the IT and telecom sector and in the process the shareholdings in Scania were to be sold. VW, as an old business ally of Scania, seemed to be the natural taker for Investor's shares.

Table 14. Heavy trucks, global market share 1996

USA, 1996	Market (%))
Freightliner/ Ford	38
Paccar	22
Navistar	17
Mack	12
Volvo	9

Europe, 1996	Market (%)
Mercedes	18
Volvo	16
Scania	15
MAN	12
Iveco	12
Renault	11
DAF/Paccar	9

Brazil	Market (%)
Scania	38
Mercedes	29
Volvo	26

Company reports

Talks were started. In 1999 VW-CEO Dr Piëch talked publicly about interest in buying Scania and also German MAN's truck division. However, the parties could not agree on a price. This left an opening for Volvo, the second large Swedish vehicle producer. Volvo's CEO Leif Johansson had approached the Wallenbergs to discuss a merger of Volvo and Scania. Scania's CEO Leif Östling had been negative, not believing in the rationale of merging two such similar and directly competing manufacturers.[108]

In a surprise and hostile move, on 15 January 1999 Volvo an-

[108] Swedish media is full of examples of Östling's negative stance on consolidation in the industry, e.g. Swärd (1999) Svenska Dagbladet, 17 January.

nounced a thirteen per cent shareholding in Scania. Volvo had bought its shares mainly from two Swedish national pension funds. There were also delicate cultural dimensions to this deal as Volvo's hostile bid on Scania was a breach of the old Swedish balance of power between the two banking spheres – Handelsbanken and Wallenbergs. The act also spurred conflicts within the close-knit Swedish business community (for a description e.g. News agency TT, 1999, 15 January; Dagens Nyheter, Sandberg, 1999, 9 March; Dagens Nyheter, Nachemson-Ekwall 1999, 12 May; Affärsvärlden, Nachemson-Ekwall, 2006, 6 December)

A deal was finally sealed on 6 August 1999, when Volvo bought Investor's shares in Scania for 315 SEK, almost double the introduction price of 180 SEK three years earlier. In the deal Investor would end up with a ten per cent shareholding in Volvo. The public bid valued Scania at SEK 60 billion. The consolidated group would produce 125 000 vehicles. Scania CEO Östling was unhappy. What remained was clearance for the deal from the European Commission.

During the autumn of 1999 Scania executives moved to Gothenburg, among them Håkan Samuelsson, often described as the crown prince to the CEO position at Scania. Now Samuelsson expected to head the merged Volvo-Scania truck division. However, in February 2000 Samuelsson was invited to head the vehicle division of MAN, MAN Nutzfahrzeuge. On 14 March 2000 EU blocked the merger between Volvo and Scania.

For shareholders in Investor and Scania the outcome was negative. Volvo had bid 315 SEK per share, valuing Scania at 60 billion SEK. On a stand-alone basis Scania's value was expected to fall back to 200–220 SEK. Volvo, having paid an average 266 SEK a share for 45 per cent of stocks and 31 per cent of the votes, would make a loss of SEK 3.5-5 billion. Investor too would be stuck with shares of less value and no deal done.

Volvo then instead merged with the vehicle division of French state-controlled Renault, Renault RVI, including its US-based truck brand, MACK truck. In the deal Renault ended up with a 20 per cent stake in Volvo. Investor acted just as quickly and sold 18.7 per cent of capital and 34 per cent of the votes in Scania to VW. That meant that VW would stay below the 40 per cent threshold for the Mandatory Bid Rule that had been enacted in Sweden in 1999.

Investor's block of A shares in Scania was sold for 370 SEK, around 100 SEK above current market price. At the press conference VW CEO Dr Piëch described Scania as the foremost heavy vehicle manufacturer in the world – "the king of the roads". Scania CEO Östling also blessed the deal (Dagens Nyheter, Nachemson-Ekwall, 2000, 28 March).

For VW the Scania investment became a disappointment. Scania and VW looked over the possibility of establishing an industrial cooperation but most of the suggestions were to be turned down by Scania. Östling simply proclaimed that synergies between the companies were lacking.[109] VW on its side was soon to be occupied with more urgent issues. In 2001, profitability was low, the share price pressed and the EU Commission was working on a takeover directive expected to overturn the WV Law. With this in mind, the VW board and CEO Dr Piëch desperately needed to increase profits, increase VW's appeal to (foreign) investors, raise the stock prise and ensure that VW became too expensive to attract interest from hostile parties. The media speculated over a sale of VW's Scania shares to MAN, Italian Fiat, American Paccar or Japanese Toyota. In this context of uncertainty, Volvo's remaining shareholding in Scania was to remain a worry for years to come.

After the break with Volvo, Scania continued working with different joint projects with other companies. As new head of MAN Nutzfahrzeuge since 2000, the former Scania director Samuelsson seemed to follow the same industrial track. The industrial logic was there. Both companies were profitable and produced 40 000 vehicles a year, a small number compared to Volvo, with its divisions Renault and Mack, totalling 157 000 vehicles and Mercedes-Daimler with 195 000 vehicles at the

[109] Leif Östling has explained the lack of synergies many times, for example Dagens Industri Dimension, Nachemson-Ekwall, 2010: "If we begin by looking at possible synergies between automotive and vehicles there aren´t any within procurement, production or sales. Francisco J Garcias Sanz (board member of Scania and member of VW's global group for procurement) and I have had many discussions about this over the years. However, there are synergies within R& D".

time. Scania produced only heavy vehicles, above 16 tonnes; MAN had both heavy vehicles and middle-range vehicles. In December 2002, the media reported that Scania and MAN were discussing joint ventures in components and parts. Volvo's shareholding in Scania had still not been sold, and the media speculated of a possible merger between MAN and Scania.

Uncertainty concerning the ownership structure of MAN had by this time become an issue in Germany. The German financial consortium holding 25 per cent of the MAN shares was, in line with the dissolution of the Deutschland AG model of control of German industry, expected to sell off their investment. The MAN board feared that new owners would attack MAN's conglomerate-like structure. In the summer of 2003 there were rumours in the German media claiming that VW had approached MAN for merger talks. New VW CEO Dr Bernd Pischetsrieder even went public stating that co-operation between MAN and Scania would be a good idea and that VW could take the role of "mediator". Scania and MAN also presented a formal cooperation agreement involving gearboxes, axles and other components.

Possible merger talks, however, remained unfruitful. With MAN's conglomerate-like structure it was impossible for Scania to establish direct ties with MAN's vehicle division, and complex German employment laws limited the potential for reconstruction and cost cutting. Plans in the German business community to break up the MAN conglomerate also fell through. These plans included a sell off of the vehicle division to VW, which could then be merged with Scania. MAN's chairman Dr Rudolf Rupprecht had opposed these plans and instead began to streamline the conglomerate.[110]

From Scania interest in merger talks remained just as tepid as before. In the autumn of 2003 Scania CEO Leif Östling was quoted as saying that Scania should be seen as a niche company (Wire service Reuters, 2003, 2 October). The most important thing for Scania was to have

[110] It was later confirmed that talks between the parties had been pursued (Affärsvärlden, Askman, 2003, 13 April; Affärsvärlden, Nachemson-Ekwall, 2003, 13 November).

competent long-term owners, which Scania had in Investor and Volkswagen. A number of initiatives were taken to entice Volvo to sell its remaining Scania shares, some involving a group of Swedish institutional investors, but nothing emerged.

In 2004 Volvo created Ainax (resembling Scania backwards), an investment company with asset made up of Scania A shares. The holding, consisting of 24.8 per cent of the votes and 13.7 per cent of shares was distributed to Volvo's shareholders in the spring of 2004. The Scania B shares were sold straight to the market. In the summer of 2004 Ainax was listed on the market place New Markets (Nya Marknader), a trading platform housing companies not yet ready for a listing on the Stockholm Stock Exchange and thus not required to obey the listing requirements. These companies did not comply with the NBK recommendation concerning flagging requirements, set at a five per cent threshold nor the Mandatory Bid Rule. The Wallenbergs and Investor used this opportunity to buy 15 per cent of shares and votes without flagging and also surpassing the 30 per cent threshold without triggering the MBR, claiming that the two not be regarded as concert parties. This caused upheaval among investors on the SSE and in the Swedish business community, especially as Claes Dahlbäck, chairman of Investor, also chaired the self-regulatory body NBK in charge of guidelines for best practise among stock-market actors (e.g. Dagens Industri, Hammarström, 2004, 15 June; Veckans Affärer, Billing, 2004, 8 November).

In the winter of 2004, Scania finally offered to buy Ainax without paying a premium. Two years later, in the summer of 2006, the Wallenberg group ownership in Scania amounted to 16.5 per cent of shares (29.9 per cent of votes). It was claimed officially that the two shareholders, i.e. Investor and the Wallenberg Foundation, were acting independently. The Swedish Securities Council never acted on any of these matters.

7.6.2 MAN's hostile bid

During 2004 and 2005 MAN moved quickly in its process of restructuring. In July 2004 MAN announced that Samuelsson, then successful head of the truck division, was to become CEO of the whole group from 1 January 2005. This spurred further speculations of closer ties between Scania and MAN. Early in 2005 MAN's largest shareholders for three decades finally sold off their shares in MAN to a group of financial institutions, turning the free float of MAN shares' on the Frankfurt Stock Exchange to nearly 100 per cent. Samuelsson was thus facing the dilemma of running a conglomerate with five different businesses, apt for a breakup, with an open shareholder structure, which made MAN an easy target for activist investors and PE funds eyeing parts of German industry. At the same time the MAN board's priority was to keep the MAN group independent and headquartered in Munich (e.g. Financial Times, Milne, 2005, 13 January).

In December 2005 Samuelsson had talks with Scania CEO Östling. The co-operative agreement of 2003 between the two parties had not delivered according to expectations, so Samuelsson suggested that the two companies instead merge and share profits between them. Östling had not been interested. Samuelsson, believing in industrial consolidation, scale, fast-moving globalization, pressing environmental and emission issues and a general need for cost reduction, decided to continue working on a merger idea alone (a recount is offered in Dagens Industri, Nachemson-Ekwall, 2006, 6 December).

In the winter of 2006 MAN enrolled Greenhill, a small investment bank that in a short time had grown to become one of the largest corporate advisors on M&A in Germany. Rumours had it that MAN had turned to Greenhill as no London-based investment bank wished to participate in a hostile bid targeting a Wallenberg company. Central in the process was also MAN's chairman Dr Eckhart Schultz, CEO of the steel company Thyssen Krupp. VW was Thyssen Krupp's largest customer and Schultz had a close relationship to VW CEO Dr Pischetsrieder.

MAN also enrolled Svenska Handelsbanken Capital Markets as an advisor in Sweden. There the designated bankers had both been working with Volvo's bid on Scania in 2000 (in previous employment at the competing investment bank of SEB) and on Scania's Ainax case in 2004. The relationship was going to become a delicate issue as Handelsbanken was

Scania's major banking contact and now would end up turning against a customer (*Ibid.*).

In the winter of 2006 Samuelsson worked with the refocusing and restructuring of MAN's conglomerate structure. He said in public that MAN would consider buying VW's shares in Scania, a block of 19 per cent, if they were for sale. Scania CEO Östling reacted in public with discontent. In the spring of 2006 cooperation between the two parties was more or less halted, and Scania's CFO also left in a surprise move, which was later shown to be related to his positive stance toward MAN.

In the late spring of 2006 the way forward for MAN and its advisors at Greenhill and Handelsbanken were to circumvent Scania's CEO Östling, by approaching Scania's twin owners, VW and Investor. Talks between Schultz and Pischetsrieder indicated that VW would support MAN. This was of importance for Handelsbanken's decision to participate in the bid plans as VW was expected to be able to pressure Investor to accept a bid from MAN.

MAN and its advisors finally had a meeting with Investor and CEO Börje Ekholm on 12 July. Samuelsson presented a deal in which MAN would buy Scania. The aim was to create a truck holding company in which the two brands – Scania and MAN Nutzfahrzeuge – would work as independent brands, very much in the same way as Volvo had organized its holding in Renault and MACK. Samuelsson proposed that Investor and Wallenberg remain shareholders. In July 2006 Scania was trading at around 340 SEK, equivalent to a market value of SEK 68 billion. The price suggested for Scania was SEK 442 per share (SEK 90 billion). Investor replied that they would consider the proposal. The MAN people felt confident that Investor would sell.

However, summer passed without Investor's reply. When CEO Samuelsson presented MAN's Q2 report in August, he spent a considerable time talking about the need for industrial consolidation. In early September VW CEO Pischetsrieder said to analysts that VW wished to participate in consolidation work. The messages got Scania rising on the stock market and going forward speculation of merger activities was to run high.

That week in September Investor CEO Ekholm finally came back to Samuelsson with the message that Investor was not interested in the MAN offer as it had been presented in July. Samuelsson's answer was that the call came too late as MAN was already preparing a bid.

On Monday 11 September 2006 MAN sent a letter to Investor, offering 442 SEK for each Scania share. MAN had tried to structure a deal so that only Investor received payment in cash and other investors, besides small retail investors, settled for payment in MAN shares. VW was expected to accept payment in MAN shares and thus emerge as the largest shareholder in MAN. MAN remained willing to pay Investor in shares, which would have given Investor the position as the largest shareholder in MAN. The same offer was sent to VW. The MAN team expected that VW CEO Dr Pischetsrieder would persuade Investor and the Wallenbergs to accept the MAN bid (*Ibid.*).

However, the Wallenbergs were taken aback by the bid, which showed that MAN had not considered Ekholm's negative stance. Instead of replying Investor passed the MAN offer over to Scania, which informed the Stockholm Stock Exchange. The following day news of the bid began to leak, and Scania stock suddenly rose almost 10 per cent in the afternoon trading on the SSE. Trading was halted and news agencies quoted anonymous sources as saying that MAN was preparing a bid. Later in the evening Scania informed the market about MAN's bid plans.

The following morning, and during the rest of the week, the media was full of articles covering different aspects of the anticipated bid. MAN's PR team had successfully marketed the merits of the deal and leaked that Wallenberg-controlled Investor had accepted a cash bid from MAN, and all that remained was a price discussion. Volkswagen was expected to remain a shareholder. Swedish, German and British newspapers wrote articles in favour of a merger that would create Europe's largest truck company (e.g. Dagens Industri, Nachemson-Ekwall, 2006, 13 September). Financial analysts also were positive. During the week MAN confirmed interest in Scania. The media wrote that MAN had developed a plan to get support from the Scania employees. MAN was to turn itself into a European SE, through which the Swedish unions would be offered seats on the MAN supervisory board, alongside the German union representatives.[111]

As it turned out media reporting during the week was flawed. Scania CEO Östling refrained from making any comments, and the Wallenbergs were upset. As the bid fight unfolded, the media also wrote that VW CEO Dr Pischetsrieder, who initially was claimed to support a bid on Scania, had not yet received support for a MAN deal from neither the VW board nor his chairman and Scania-friendly Dr Piëch (e.g. TT Wire service, Goksör, 2006, 22 September; Financial Times, Mackintosh & Milne, 2006, 26 September; Dagens Industri, Nachemson-Ekwall, 2006, 28 September).

During the weekend of 16–17 September all involved parties held different meetings. Monday morning, VW and Investor jointly decided that they would turn down the MAN offer. VW said it would only support a bid from MAN if it received the blessing of the Wallenbergs. The Scania board, also negative, had discussed different alternatives, including a buy out by a private equity actor, a merger with a competitor such as US Paccar or even a reversed bid, where Scania in a joint action with Investor and VW made a counter bid on MAN instead. For MAN the situation with a truly hostile bid was delicate. In classical investment banking jargon MAN would now be "in play", open for a hostile bid if it either withdrew its bid for Scania or the bid was turned down later.

Reasoning that it was left with no choice, MAN went public with its bid Monday morning, offering 442 SEK, SEK 88 billion (€ 9.6 billion) in total, then the largest cash-bid ever at the SSE. MAN also flagged for 2.8 per cent of the shares and 5.2 per cent of the votes, a holding equivalent to French Renault's block of shares in Scania.[112] Samuelsson said that the combination would deliver significant value to both Scania and MAN shareholders, increase competitiveness and secure jobs in Germa-

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[111] There was massive coverage in all large media sources in Sweden, Germany and the UK. Among active authors was Nachemson-Ekwall, Dagens Industri.

[112] The holding was a rest from the complex Volvo-Scania discussion after which Volvo merged with Renault's vehicle company. Renualt became a shareholder in Volvo and received Scania-shares after a complicated sell out of Volvo's shareholding in Scania.

ny and Sweden (Dagens Industri, Nachemson-Ekwall, 2006, 16 September). MAN was targeting synergies of SEK 4.5 billion (€ 500 million).

The Scania board, VW and Investor all immediately rejected the bid. Short-term investors such as hedge funds, arbitrage investors, merger funds and other speculators rushed to the Scania share, prepared for a bid-fight. The question was how to get Investor and the Wallenbergs to change their mind and accept, as most rumours indicated, a higher offer. Others were betting on a counterbid on MAN, by Scania, alone or together with Investor, or by VW.

However, there was more to Investor's rejection. The Wallenberg family had ”serious reservations” about German corporate governance and the limited influence that supervisory boards could exert over a company's operations. Investor and the Wallenbergs did not give MAN's plans to turn the merged entity into a European SE any merit. Rumours and leaks would continue for weeks, with the share price of MAN and Scania moving up or down, depending on the nature of the information (see e.g. Dagens Industri, Nachemson-Ekwall, 2006, 6 December).

A week after the MAN bid had been presented in public, on Monday 25 September, Scania CEO Östling and two of the independent directors on the Scania board (i.e. independent of both the Wallenbergs and VW) hosted a dinner for a group of asset managers and other institutional investors. Östling had warned that there were few examples of successful mergers when it came to real performance. Östling did not wish to discuss synergies, as that focus would reduce the MAN bid to a discussion of price and result in a sell out. The Scania CEO wanted investors to focus on Scania's long-term prospects including a perceived bright future for growth in Eastern Europe.

Late September, VW CEO Pischetsrieder, generally regarded as “kingmaker”, gave his only interview on the Scania topic. Talking to the Financial Times, Pischetsrieder said that he was supportive to the principle of combining Scania and MAN, together with VW's Brazilian heavy truck business, but he urged MAN to abandon its hostile bid on Scania in favour of private talks (Financial Times, Mackintosh & Milne, 2006, 26 September). The stock market reaction to the interview was to lower the price of Scania and raise the MAN stock. The directions of trade revealed market expectations that the bid on Scania would fail, which would lead to some other actor targeting MAN for a break up. Next, it was rumoured in the media that MAN and VW had agreed to merge VW's Brazilian vehicle business with MAN and Scania.

In early October the bid fight took a new turn. In a surprise move VW bought 15 per cent of the shares in MAN. With that stake, and its previous holding in Scania, VW would be guaranteed 25 per cent in the new MAN-constellation if the combined share and cash offer went through. With the chance of a bid on MAN suddenly less likely, MAN shares fell. Scania, again targeted for a takeover, rose and was again trading well above the MAN bid.

VW said in a press release that it hoped to be able to support the industrial logic of creating synergies between MAN and Scania, including VW's Brazilian heavy-truck assets. Once again VW rejected a hostile approach. The official comment from MAN was to welcome Volkswagen as a strategic shareholder. Rumours now had it that the Scania board would recommend an offer above 500 SEK, valuing Scania at SEK 100 billion (e.g. Dagens Industri, Björk, Jonsson & Nachemson-Ekwall, 2006, 6 October). In a public statement VW gave the two parties four weeks to negotiate. But the complications just seemed to continue, and actors on the stock market, as well as the media, had difficulty grasping the meaning of all the VW activity in MAN, the stance of Investor, the role of the different members of the VW board and MAN's plans. During the second week of October German Handelsblatt wrote that VW chair Dr Piëch objected to a complicated deal involving the MAN conglomerate, preferring a straight deal involving only Scania and MAN's truck division (cited in Dagens Industri, 2006, 11 October). Such a deal would clearly put Scania on top and result in a break up of MAN.

The stock market continued to be taken by surprise. The MAN team seemed to have realised that they had to act or lose out. On the eve of November 5, MAN launched a "dawn raid", buying 11 per cent of the voting stock in Scania from mainly Swedish institutional investors, including Alecta (one of the large collective pension funds). The institutions were offered a price of 475 SEK, 33 SEK above the previous bid price. They were also offered a top-up deal, which included the difference if

MAN later would increase the bid even further. Together with VW that meant the Germans controlled over 50 per cent of the votes in Scania. MAN then raised the bid to 475 SEK, thus valuing the whole of Scania at SEK 95 billion.

The important seller in the raid was Alecta, a corporatist pension fund jointly controlled by the Confederation of Swedish Enterprise (SN) and a group of unions organizing white-collar workers (SIF). The move had encouraged other investors, such as Swedbank Robur, to sell too. Three institutional investors of importance remained loyal to Investor and Scania. These were AMF Pension (i.e. the other corporatist pension fund run jointly by SN and the workers union, LO), Nordea and SEB Trygg Liv.

The Scania board still rejected MAN's offer claiming it "substantially undervalued Scania". According to the board the earnings outlook for the stand-alone company was "significantly above current market consensus", and MAN's announced synergies materially underestimated the true synergy potential of a combination of Scania and MAN. As a tactical move, the Scania board planned for a review of Scania's capital requirement, targeting a distribution of an additional amount of up to SEK 10,000 million (including ordinary dividend).

The Wallenbergs and Investor were upset, but acted with more care, keen to not be accused of not acting in the interest of all shareholders (something which would be reflected in the share price of the investment company Investor trading at a discount to net asset value). Now CEO Ekholm said that there were industrial merits to a merger but synergies were well over SEK 10 billion (one billion euro) – over a time period of a few years (Newswire Direkt, 2006, 12 October). According to Ekholm it was the responsibility of the Scania board to ensure that the Scania management deliver this potential in co-operation with MAN or present an alternative development plan.

Leaks to the media continued to point in different directions. Whereas the Swedish media became focused more and more on the hostile fight, the German media together with the Financial Times wrote that VW was moving in favour of MAN. There were also rumours that VW planned to buy additional shares in MAN (e.g. Financial Times, Milne, 2006, 13, 14 & 15 October; Dagens Nyheter, Gripenberg, 2006, 8 November; German weekly Focus, 2006, 6 November)

The VW supervisory board had a meeting on Sunday 15 October, three days after MAN's surprise raid to acquire 15 per cent of the shares in Scania. Afterwards the VW board said it was ready to support a bid from MAN if it won approval from Scania and Investor. It also said that it would not support a hostile counter bid from the two parties. MAN "welcomed the VW announcement". That decision carried a one-month deadline, until November 16.

The plan from the VW supervisory board was to set up a new holding company into which both truck makers would be moved, treating the deal as a merger rather than a takeover. But the consensus among the VW directors was to remain fragile. On 27 October VW increased its stake in MAN to 20 per cent and received permission from the German financial authority, BaFin, to increase its shareholding to just below 30 per cent, thus cementing de facto control over MAN.

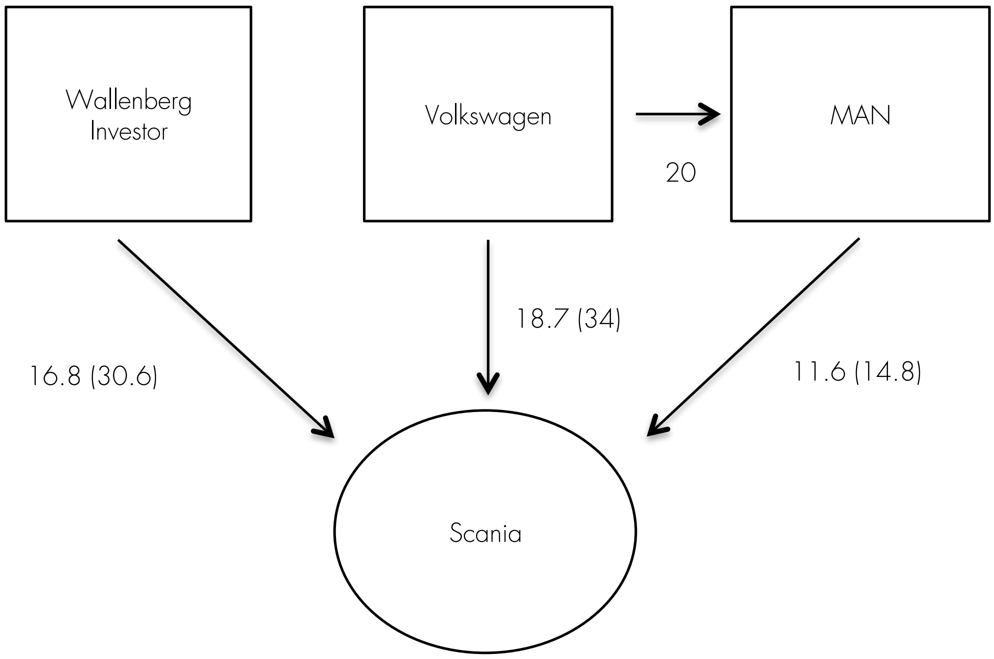
On November 6 MAN finally presented its offer document, supported by financial advisors Handelsbanken, Greenhill and Citigroup. There were immediate complaints that MAN had excluded information that Investor and the Wallenberg Foundation had rejected the offer. The same day the German media spread rumours that the Federal State of Lower Saxony, controlling around 20 per cent of the shares in VW, had offered MAN half of its position in VW. A crossholding between MAN and VW, praised by Lower Saxony, would imply that MAN could remain with its conglomerate-like structure while VW and VW's Dr CEO Pischetsrieder could remain independent from both Porsche and VW chairman Piëch. The planned three-party deal was never confirmed and never sealed. The deal also mirrored the complicated political dimension related to Porsche's role as owner of VW at a time when the EU was targeting the VW Law.

On 7 November VW issued a press release stating that CEO Dr Pischetsrieder had agreed to resign as of 1 January 2007, to be replaced by Martin Winterkorn, currently successful head of VW's Audi brand and generally seen as a Piëch protégé. The true reason for the dismissal of CEO Dr Pischetsrieder was never clarified. Different theories were presented in the media that taken together pointed to Dr Piëch having taken an opportunity to team up with frustrated union representatives on the VW board to oust Dr Pischetsrieder (see e.g. German Focus, cited in Dagens Nyheter, 2006, 6 November; Financial Times, Betts & Milne, 2006, 8 November).

Going forward, the German corporate in-fight over the soon to be abandoned VW Law, along with the surprise dismissal of VW CEO Dr Pischetsrieder, was thus to have a profound effect on MAN's bid fight for Scania. What appeared to have started as a friendly alliance between the MAN CEO, Samuelsson, and VW's CEO Dr Pischetsrieder in a discussion over the control of Swedish Scania, had now thrown MAN into the arms of VW chairman Dr Piëch instead. On 8 November Porsche publicly announced interest in increasing its shareholding in VW from 21 per cent to maximum 29.9 per cent. It was interpreted as a clear answer to actions taken by the Federal State of Lower Saxony.

During the period to come Scania embarked on a defensive campaign. There was a public attack on German corporate-governance practises, with its enhanced position for workers, interrelated two-tier board structure and state-controlled golden share in VW. On 7 November, Investor flagged having bought an additional 0.3 per cent of capital and 0.7 per cent of shares in Scania. It was just a slight increase, but a symbolic gesture that the Wallenbergs past control of 30 per cent of the votes (*Figure 12*). Investor paid 519 SEK a share, well above MAN's increased offer of 474 SEK. On 17 December the Swedish Securities Council surprised market actors with granting Investor and the Wallenberg funds an exemption to the Mandatory Bid Rule, claiming that the joint shareholding did not surpass VW's ownership of 34 per cent of the voting power in Scania and thus was not considered as altering the position of minority shareholders. At the same time Scania unions objected to the possible merger, as MAN's union contracts would weaken the position of Swedish workers. Then the Scania board published a defence document with growth prospects and detailed calculations of Scania's value.

Figure 12. Ownership of Scania 11/11/06: capital (votes)



SIS Ägarservice (2006)

The Scania board claimed that Scania was worth as much as 557 SEK a share, or SEK 111 billion. The Scania board also filed protests to the SSE and the Securities Council. Scania CEO Östling attacked MAN and Samuelsson in public. In the aggravated process light was also shed on the delicate relationship between Handelsbanken's investment bank, Scania and Investor. This did not stop incumbent Scania-shareholders from selling shares during the autumn. As of 31 October Swedish investors had reduced their stake from 59 per cent to around 40 per cent, the buyers mainly being foreign hedge funds and arbitrage investors trading on the price differential between MAN and Scania.

Scania held a Capital Markets day on 6 December. The executive management team presented a very positive outlook: CEO Östling talked about his discontent with the situation, and he warned of "anti German" feelings in Sweden. Östling described Samuelsson as a "traitor" and "persona non grata" at Scania, and then went on to criticize the activities of MAN's chairman Dr Schultz. With VW CEO Dr Pischetsrieder out of the picture, Östling claimed that Dr Schultz should withdraw the bid and that VW the following spring replace some of the directors of MAN with people ready to reconsider MAN's conglomerate-like structure. That would increase chances of a deal directly between the two vehicle companies, according to Östling.

The Scania-MAN matter also led to comments from Sweden's new right-of-centre government. During a press briefing new prime minister Fredrik Reinfeldt said that he hoped that there was a long-term ownership-responsibility in place in Sweden concerning Scania, "…to allow this crown jewel of Swedish industry to remain with its headquarter in Sweden also in the future…"(Wire service Direkt, 2006, 7 December).

MAN made a last attempt to save the bid. The acceptance period was prolonged from 11 December to 31 January 2007. At the same time MAN announced that it hade received a credit facility of € 11 billion, three billion more than the offer, from a consortium of investment banks consisting mainly of Citigroup, the Royal Bank of Scotland and Handelsbanken.

During Christmas and New Year there were various rumours that VW and its new CEO Dr Winterkorn was about to change sides and join MAN. There were rumours of a bid rise to 520–530 SEK. However, on 11 January 2007 VW publicly rejected the MAN offer of 475 SEK per share. At the same time VW announced a new strategy, changes in its own management team and a new focus on the truck business (e.g. Affärsvärlden, Östlund, 2006, 20 December; Wire service Direkt, Hägerstrand, 2007, 10 January).

The development was unfavourable to MAN. MAN did not have a plan ready to tackle a situation in which both the bid fell through and VW declared an interest in MAN. Discussions between the three parties, VW, MAN and Investor, were carried out in the first weeks of 2007. At a meeting in Stockholm on 15 January, the Wallenbergs and Dr Piëch made clear that they would not accept a bid, no matter the level. The media wrote that MAN had been discussing raising the bid to 525 SEK (Frankfurt Allgemeine Zeitung, 2007, 13 January). On 17 January hedge funds gave up their speculation, and began to sell off Scania shares (Dagens Industri, Nachemson-Ekwall, 2006, 18 January).

The MAN offer on Scania was formally set to last until 31 January, but MAN decided to withdraw it on 23 January. Swedish Prime Minister Fredrik Reinfeldt welcomed the move in a comment (Newswire TT, 2007, 24 January). Scania unions, Investor and the Scania board all gave comments stating that they looked forward to friendly discussions. The MAN supervisory board declared its full support for further proceedings and expressed their complete trust in CEO Samuelsson. In Sweden MAN's agreement with Handelsbanken led to bitter repercussions, as Scania and Investor threatened to terminate various business relations with the bank. The Handelsbanken CEO, Boman, publicly stated that the bank regretted the activities pursued by the investment bank division. The two leading advisors involved left the bank.

7.6.3 VW's power play

This did not end the power struggle over Scania. It merely changed its profile as VW took a more active role than it had done previously. As early as in the winter of 2007 VW turned to the Swedish Securities Council asking if it would be allowed to increase its stake in Scania from 34 per cent to 49.9 per cent, without being mandated to apply the Mandatory Bid Rule (MBR). An exception was granted. In March VW declared that it had increased its shareholding in Scania from 18.7 per cent to 20.03 per cent, representing 35.31 of the voting rights. The Securities Council had argued that the activity did not result in a de facto change of control. Market actors were taken by surprise. However, at the time minority investors in Scania were comforted by a public promise from the Wallenberg's to continue to act in the interest of "all shareholders" (as stated in the Q2 report).

At the time of the Scania AGM on 3 May VW had further increased its voting power in Scania to 36.4 per cent. Added to MAN's 14.8 per cent of the votes, the total German vote was 51.2 per cent. Winterkorn was elected new chairman and Investor CEO Ekholm was elected new deputy chairman. VW also strengthened its presence in MAN, having Dr Piëch replacing Dr Schultz as chairman, and letting the latter take the role as deputy chairman. Two more VW directors were also elected to the MAN board.

Early autumn 2007 VW once again tested the Swedish MBR, this time asking for assurance that MAN and VW were treated as unrelated parties and that VW, in accordance with the Swedish MBR would be allowed to continue buying Scania shares also beyond the 50 per cent threshold. The Securities Council would later also determined that the exception granted VW would include VW's ownership in MAN as well.

The media wrote about the decision, quoting puzzled investors and analysts. However, the general view was that as long as the Wallenbergs remained as shareholders the power balance would remain. However, this time the Wallenbergs had serious concern over the council's ruling and VW's actions, writing in the Q3 report on 11 October that the Investor strategy was not to be the largest minority investor and that Investor would attempt to find a long-term industrial solution for Scania while maximizing the value for "our" shareholders, and not "all" shareholders which had been the wording in statements from the spring. Dagens Industri highlighted the changed wording in an article on 18 October, claiming that VW and Scania had agreed on a plan for a Scania takeover of MAN, the question not being if, but when. For the Wallenbergs the options was to either remain a shareholder in a combined entity, or make VW pay a premium for its shares and leave (Dagens Industri, Nachemson-Ekwall, 2007, 29 September, 18 October).

Shortly before Christmas 2007 MAN flagged for an increase in its Scania holding from 14.8 per cent to 15.6 per cent of capital. Among the shareholders that had taken the opportunity to trade more valuable A shares in exchange for lower-priced B shares was the retail fund Robur, part of Swedbank. After New Year Investor CEO Ekholm openly complained about the way the Swedish Securities Council had interpreted the MBR, warning that VW might control the whole Scania board at the next AGM.

During a few weeks in January and February 2008 there were talks between VW and Investor. Rumours on the stock market continued, and the spread between the Scania A and B shares widened (e.g. Dagens Industri, Svensson, 2008, 19 January). MAN bought additional shares, increasing its ownership to 17 per cent. This time AMF, the corporatist pension fund run jointly by the Confederation of Swedish Enterprise and the Blue-collar workers (LO), traded higher valued A shares for lower valued B shares. The chairman of the metalworkers' union, IF Metal, complained that the AMF management lacked competence to act in long-term interest of Swedish industry and was only focused on short-term profits and trading.

On 3 March 2008 VW bought the Wallenberg's shares in Scania. VW's investment in Scania grew to 37.7 per cent of capital and 68.6 per cent of the votes. MAN already owned 13.2 per cent of capital and 17 per cent of the votes in Scania. At the same time VW owned 28.7 per cent of capital and 29.9 per cent of votes in MAN. VW paid 200 SEK a share, a price the reflecting a premium of 33 per cent of market price the previous day. The stock market announcement triggered a rally in the Scania share lifting them 20 SEK to 170 SEK before a representative from Securities Council announced that VW had received an exception from the MBR.[113] Uninformed investors reacted with disappointment, if not shock, dropping the Scania share as low as 134 SEK, allowing for the interpretation that the Wallenbergs had received a 44 per cent premium on the market price paid to minority shareholders.

Statements from VW the same day were friendly, claiming the purchase of Scania shares to be an important step towards clarifying the long-term shareholder structure of Scania. CEO Winterkorn was quoted as saying that VW planned to comply with Swedish corporate-governance practice, including strong independent representation on the Scania board.

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[113] The Swedish Financial Authority discussed the VW exception from the Mandatory Bid Rule in a statement of April 10 2008, (*Sw:* "MAN behöver inte lägga bud på Scania"). According to SFSA it could be claimed that MAN's holding should be added to VW's holding, which would then trigger the Mandatory Bid Rule. However as no party had objected to the decision by the Securities Council, SFSA could not act on its own. To this was added that VW in the next step was not to be hit by the MBR as VW had already been granted a general exception to the MBR.

Swedish institutional investors complained that the Wallenberg and VW had neglected their responsibility to minority shareholders and damaged the reputation of the SSE (Dagens Nyheter, Andersson, Lagerqvist, Norman & Grefbäck, 2008, 5 April). The Swedish Shareholders Association claimed that through their sell off the Wallenbergs had lost legitimacy in Swedish society. The media quoted Swedish industrialists critical of the Wallenberg's actions (e.g. Dagens Industri, 2008, 19 March). Demands were voiced for new thresholds of the MBR set at 50 and 67 per cent, just like in many other EU countries (Dagens Industri, 2006, Swedish Shareholders Association, 7 March). Investor CEO Ekholm defended the activity saying that Investor had a responsibility to its own 130 000 shareholders (making up 75 per cent of capital and 50 per cent of the votes in Investor). VW had been granted an exception to the Mandatory Bid Rule, which left Investor with no choice but to sell its shares to VW when they offered a good price. Scania CEO Östling welcomed VW as owner, something that brought a ten-year period of uncertainty to a halt. In May 2008 VW signed a new employment agreement with Östling, prolonging his employment to 2012.

7.6.4 Aftermath

VW's share increase in Scania was paralleled by a closer and in many senses much more startling relationship between Porsche and VW. In 2007 the European Court of Justice finally deemed the VW Law an illegal protective device. Following that, through a number of controversial and unorthodox moves, Porsche gained control over VW.[114] In a parallel process VW chairman Dr Piëch ousted his relatives in Porsche. The struggle involved a highly disputed options and share transaction in 2008, at the height of the financial bubble, where Porsche through a highly leveraged (and risky) transaction ended up with over 50 per cent of the shares in VW. The transactions were brought to a halt in the autumn of 2008 when the US investment bank Lehman crashed, and the

[114] A detailed recount of this fascinating power struggle is offered in Nachemson-Ekwall (Scania, unpublished manuscript, 2012)

turmoil spreading through globalized financial markets and also hit the financial situation of Porsche. The deal involved huge losses for a number of speculators and hedge funds and in the aftermath of the crash a number of court cases were opened. The Porsche CEO and CFO were replaced in 2009. Following a complicated rescue plan involving financial support from the sovereign wealth fund of the Arab state of Qatar and the German government, Porsche and VW were merged to create an "integrated automotive group" supervised by Chairman Dr Piëch.

The industrial transformation of MAN continued with Samuelsson selling off large subsidiaries to streamline the business group. MAN also embarked on an expansion eastwards into India, China and Russia. In December 2008 MAN bought VW's Brazilian truck and bus operations, turning MAN into the world's third largest commercial vehicle producer behind Volvo and Daimler-Chrysler.

Porsche's approach to VW in the autumn of 2008 also resulted in a rally of the shares in Scania as it meant that there soon would be a change in control of VW, thus triggering a mandatory bid on Scania. A minimum bid-price resulted in Porsche getting hold of 7.9 per cent of capital, and 2.3 per cent of votes. The shares were resold to VW, which increased its shareholding in Scania to 49.3 per cent of shares and 71.9 per cent of votes.

In the autumn of 2009 VW began working on plans to create an integrated car and truck empire. Now chairman Piëch talked openly about adding another two vehicle brands to the ten marques it was to own after VW had merged with Porsche. On 24 November 2009, Samuelsson resigned after nine years at MAN. The surprise decision created opportunities for the chairman. Within a period of one week MAN's CEO, CFO and the head of the vehicle division were all dismissed. VW also announced plans to form a specific vehicle division consisting of VW's shareholdings in MAN and Scania. Again there were rumours of a three-party merger.

In spring 2010 VW strengthened its control over the Scania board by replacing independent directors Bohman and Bruzelius with two VW directors. This meant that the by VW suggested newly elected legal director Thunman together with Ekholm, CEO of Investor, and Peter Jr.

Wallenberg, from the Wallenberg Foundation, would remain as the only independent directors on the Scania board (despite having sold all their shareholdings). This action resulted in upheaval in the Scania nomination committee, with Swedbank Robur and Alecta resigning in protest over what they declared to be a breach of the Swedish Corporate Governance Code. At the Scania AGM in May, VW CEO and Scania chairman Winterkorn apologized for what had happened, saying that the board would continue working to maximize long-term value for all shareholders.

From a Swedish perspective these board moves were interpreted as the last chapter of what had been a ten-year struggle over control of the Swedish heavy vehicle champion. In early July Volkswagen announced the final establishment of a new “Group Trucks” within VW. In late July 2010 Scania and MAN also announced plans to start a study on the potential for collaboration on component supply and pre-development. As a parallel move, VW continued its work to strengthen control over Porsche and by 1 March 2011, VW finally completed the merger with Porsche, which at the same time made a rights issue to cut back its high net debt from previous years.

In 2011 and 2012 Volkswagen continued to work for the strengthening of the relationship between MAN, Scania and VW. Östling’s position as CEO of Scania was extended for three more years to 31 March 2015, when Östling would turn 70. In the summer of 2011 VW increased its shareholding in MAN above 30 percent, thus triggering the MBR. VW commented ”This means that Volkswagen has reached an important milestone on the way to creating an integrated commercial vehicle group and is closer to its goal of leveraging substantial synergies between MAN, Scania and VW in the interests of all its shareholders, employees and customers” The offer to MAN’s shareholders gave VW control of 56 percent of the voting rights and 54 percent of the capital of MAN.

To accelerate cooperation between Scania and MAN, Volkswagen tried to appoint three VW managers and directors that were also on the Scania board as directors also of MAN. This move, a clear breach of the German Corporate Governance Code, was met by protests from MAN’s minority shareholders. At the time of the AGM VW decided to withdraw the three candidates. But that did not stop VW. In the spring of 2012, VW took full control of the Scania board with five out of seven directors related to VW. Following that Östling after 23 years as CEO of Scania was offered a directorship on the VW Executive Committee and was replaced as CEO by one of his adepts. Another Östling adept was offered the position as CEO of MAN. Thus the tri-party merger was finally sealed with a full integration on the management side, leaving the remaining minority shareholders in MAN and Scania aside.

7.7 Analysis of the Scania case

Just like the Skandia and Capio cases, the Scania study reveals three parallel contingencies that can be said to impact a cross-border hostile-takeover process in the era of financial capitalism: the Swedish model of corporate governance, short-termism among institutional investors and regulatory and moral arbitrage. However, given that the Scania fight both involved Swedish controlling shareholders and Continental stakeholder governance, there are certain differences that change the framework and broaden the perspective. As the Scania fight developed it came to reflect (1) differences between German and Swedish corporate governance regimes, (2) arbitrage, cultural and regulatory as well as moral between national takeover rules, especially relating to the Mandatory Bid Rule. The fights also revealed tendencies towards (3) breach of trust and short-termism among both controlling shareholders and institutional investors in their position as minority shareholders. These are analysed more fully below.

7.7.1 Conflicting German and Swedish governance models

National differences in corporate-governance procedures had significant influence on the outcome of the Scania fight. This was true of the relationship between MAN and Scania, MAN and Volkswagen as well as between Volkswagen and Scania. The German stakeholder-governance model, co-determination and with national union representatives present on the boards and empowered with the rights to block certain decisions, including lay-offs and closures of corporate production sites, differed from the more symbolic board influence by the Scania unions. The Swedish local union representatives could only exercise influence through gaining public support for its opposing views from the national unions and politicians.

Scania also involves a cross-border fight among companies governed by dramatically different models of corporate governance. Despite the corporatist communality embedded in the two welfare states, Swedish governance and the Companies Act have a clear shareholder orientation whereas German governance and the Company Law have a stakeholder orientation. Shareholders of a German listed company cast votes for directors on five-years tenure. Thus MAN emerged with a dispersed shareholder structure but in a stakeholder regime rather than a Swedish shareholder regime (compare Skandia). This was also exemplified by MAN's plans to reincorporate itself into a European company, Societas Europea, with a regulatory framework more able to facilitate corporate restructuring through merger activities across national borders. From the Swedish directors' horizon the stakeholder issue would remain, with unions occupying the equivalent number of boardroom seats as the shareholder representatives. From the unions' perspective the employment security offered workers at certain German employment sites would remain unchanged. The German stakeholder perspective also governed the position taken by the MAN chairman, who acted to assure that MAN remained a conglomerate and headquartered in the Federal State of Bavaria. The board of Scania claimed to act in the interest of all shareholders when turning down the MAN bid, but given the VW exception to the MBR the outcome came to reflect the problem related to a controlling shareholder channelling the bidder's (VW's) takeover premium into its own pocket. There was also an interesting German governance twist to the ousting of VW CEO Bernd Piechtrieder in the autumn of 2006. The work by the VW CEO to enhance the firm's profitability, in the proclaimed interest of all shareholders, against the interest of the union board representatives, appeared to have been successfully exploited by VW chairman Dr Ferdinand Piëch both to remove the CEO and to gain control over VW himself.

On the Scania board, with directors representing the largest shareholders, including the Wallenbergs, Volkswagen's acquisition of the Wallenberg stake of A shares put a special twist to the agency conflict between the blockholder and the minority shareholders. The Swedish model of corporate governance implicitly presupposes that the blockholder acts in the interest of all shareholders alike and as such is ready to bargain for the shareholders as a group (Burkart and Panunzi, 2007). This was not the case when Investor and the Wallenberg's accepted the bid from VW in 2008 and left the minority shareholders without a premium. As such, the Wallenberg's role became double edged, if not triple edged, with Wallenberg directors on the Scania board having to act in the interest of all shareholders alike while Investor and its directors at the same time acted in the interest of Investor's own shareholders, which included the Wallenberg Foundation that also had board representation on Scania. This also means that the Scania defence document fell short of protecting minority shareholders from VW.

Other examples of governance differences relate to the enrolment of directors on the board and the work of the Swedish nomination committee. The Volkswagen CEO said at the time of the purchase of Investor's and the Wallenbergs holding in Scania in February 2008 that VW would act in line with Swedish governance procedures. However at the AGM in 2010 VW acted against the interest of the two Swedish institutional investors present on the nomination committee, dismissed the independent deputy chairman of the board and nominated a VW director in his place, thus taking control of both the chairman and the deputy chairman positions. VW also nominated a Swedish director with legal expertise, a common background for a German director but not in Sweden as that expertise is expected to be present either through the board secretary or dealt with in relation to specific issues. The other two independent directors on the Scania board were the CEO of Investor and a director of the Wallenberg Foundation, representing two investors that had sold off their investment two years earlier. Thus the Scania board remained in firm control of VW, a clear breach of Swedish governance principles. The procedure was repeated at the 2012 AGM.[115] The minority shareholders in MAN had a similar experience.

7.7.2 Regulatory and moral arbitrage

An example of regulatory arbitrage in the Scania case involves the golden share in Volkswagen. Volkswagen, under the control of the Federal State of Lower Saxony, bought Scania shares without any concern of being a target itself. The procedure was repeated when VW bought shares in MAN. This form of regulatory arbitrage also created opportunities of cultural and moral arbitrage when the struggle for corporate control moved from the executive (management agent in Scania, Volvo, MAN and VW) to the ultimate controller (principals represented by Chairman Dr Piëch in VW and Wallenberg Sr., the ultimate head of the Wallenbergs in Investor). This move can also be described as an agency conflict between the controlling blockholder and minority shareholders, as the controlling-blockholder actors move from a previous societal context of close-knit societies (banking governance in Germany and industrial governance in Sweden with reliance on a system with multiple voting rights) to the rationality of financial capitalism (Kallifatides, Nachemson-Ekwall & Sjöstrand, 2010).

[115] The misuse by VW of the nomination committee continued ahead of the AGM in 2012 when the two largest Swedish institutional investors, Alecta and Swedbank again refrained from participating. On April 3, 2012, Investor CEO Ekholm announced that he would resign. He was to be replaced by Peter Abele, previously in the management and on the board of the VW brand Audi. On April 30, 2012 Scania announced that Dr Piëch would be nominated as chairman, thus chairing MAN, VW and Scania at the same time. In addition director Larsson was to resign. Thus, left as independent directors on the Scania board were Åsa Thunhammar, a corporate lawyer, and Peter Wallenberg Jr., from the Wallenberg foundation, a minimum requirement according to the Swedish code but as both were suggested by VW and both lack industrial competence to challenge the VW directors, they gave a very weak impression of being able to act ”independently”, and the Swedish institutional investors complained at the AGM (e.g. Hägerstedt, May 4, 2012, Dagens Industri).

The Scania case also involves arbitrage related to the Mandatory Bid Rule, MBR. All in all the case reveals at least fifteen circumventions of the intention behind the MBR (for a detailed discussion see Ch. 8.9 and *Table 16*). Some of these were legally acceptable but still believed by the Swedish business community to be a breach of the rule's intention, that is to offer an equal price to all shareholders when a controlling party surpasses 30 per cent control of votes or shares. Related to the circumvention of the MBR, is also the possible circumvention of flagging requirements. Examples of these circumventions relate to Investor's and the Wallenberg funds' activities in Ainax, and to Porsche's hidden option trading in VW. Both can be seen as examples of hidden and gradual acquisitions of shares in a strategy often described as "creeping takeovers". There were also a number of incidents where VW and the Wallenbergs were granted exceptions to the MBR rule on dubious grounds in the eyes of the minority shareholders. In many MBR cases it appeared to be difficult to foresee the stance taken by the Swedish Securities Council. It appears that the council as a general rule chooses to decide in favour of a party that somehow had already surpassed the trigger treshold.

The issue of the MBR and the VW Law can together be used to highlight the role played by the incumbent corporate elites in the national implementation of EU regulation. Here representatives of the European block holder governance model, the Wallenbergs and Piech both participated in the setting of the rules and circumvention of the intention of the rules when they were in place. The Wallenbergs and Piech acted together with Swedish and German state representatives when the Takeover Directive was passed in the European Parliament. Both influenced how the rules were implemented in the national legislation and self-regulation. Both were also active in circumventing the MBR.[116]

[116] It is fair here to mention that the Swedish Social Democratic government had acted in support of the Swedish model with multiple voting rights during the work with the 13th Takeover Directive (see also Section 5.3).

7.7.3 Agency conflicts of institutional investors and blockholders

The Scania case includes a number of examples of institutional investors acting as facilitators of deals. These activities range from selling shares to Volvo in 1999 (when for example two Swedish national pension funds sold their shares) to the participation in MAN's dawn raid in November 2006 (when Alecta sold its holding) to the arbitrage trading of A and B shares in late 2007 and early 2008 (by the retail fund Swedbank Robur and pension company AMF). Arbitrage strategies by institutional investors were also evident in MAN and VW at the time of the Porsche futures trade activities. Notably, Swedish institutional investors never acted to increase their shareholding in Scania, which was made clear when Volvo searched for a buyer of its shareholding in Scania.

From the perspective of the institutional investors the European Commission's work to level the playing field and facilitate financial activities across borders appears, with Scania as a case, to have been successful. However, from the perspective of the controlling blockholder it seems that these institutional investors both used and misused the index tracking and short-term application of a financial portfolio allocation rationale to reach their goals rather than any engagement with the operational prospects of the involved companies. As such it became the block holder that mastered the power play of the financial market that succeeded. In this Scania case this happened to be the management team loyal to VW chairman Dr Piëch, who became the incontestable kingmaker of the commercial vehicle industry.

This "breach of trust" also included Investor and the Wallenbergs. They acted behind the backs of the institutional investors a number of times during the process. The first example can be said to have been the sale to VW back in 2000, the second time was the Ainax deal and the third time the sell off to VW in 2008. Notably Investor changed the wording related to the Scania investment a number of times during 2006–2008, from acting in the interest of "all shareholders" to acting in the interest of "the shareholders in Investor".

The investment banks play a role as facilitators of these deals on the financial markets. An example of this is the decision by the investment bank at Handelsbanken to participate in the preparation of MAN's hostile bid on Scania, a large customer, and aid in the financial package of MAN. Another example is the activity by the investment bank at Swedbank in the preparation of the Volvo raid on Scania in 1999. A third example is the bank consortium that participated in the Porsche options trade in Volkswagen in 2008.

Summing up, the Scania case seems to highlight the lack of convergence of European regimes of corporate governance. The actors in the Scania deal had to contend with a changing institutional context involving the transformation from a blockholder control structure with stakeholder owners loyal to societal expectations of a small country, to a globalized market of free movement of capital with international institutional investors, Americanized investment banks and corporate owners (including board members and executive management teams) loyal to the capital market's focus on shareholder-value governance. The Scania case and the outcome of MAN's cross-border hostile bid in 2006 also seems to reflect a corporate-control struggle where the institutional framework of financial capitalism (investment banks, legal regimes, short-term institutional investors) can be viewed as a trigger. The outcome, with VW on top, did not reveal the emergence of a level playing field among corporate actors. Rather, the VW–MAN–Scania deal seems to give ample evidence that in financial capitalism it is the actor that has the power to arbitrage between different governance regimes and regulatory systems that will emerge as winner.

7.8 Conclusion

This chapter has presented case studies of three highly publicized cross-border hostile takeovers involving Swedish targets during the sixth takeover wave, 2004–2008. The studies have been framed by institutionally oriented theories of the economy claiming that the outcome of a cross-border hostile bid reflects a social order where corporations are seen as institutions embedded in society. This view contrasts with mainstream finance with its idea that there exists an efficient market for corporate control and that common regulations can create a "level playing field" among corporate actors across the European Union. The purpose of the case studies has been to explore the validity of the three hypotheses developed in Ch. 6.8 related to a cross-border hostile takeover process in financial capitalism. These address the Swedish corporate model of owner governance, the role of institutional investors and their short-termist investment style and actors' ability to pursue arbitrage, both regulatory between different soft and hard laws, and moral, between different cultural and historical value systems.

The Old Mutual-Skandia case (2005) is embedded in Sweden's transformation from industrial to financial capitalism and the opening of previously captive capital markets. The actors and forces involved appear to be far from those at work on a so-called "efficient market for corporate control" (Manne, 1965). Rather the outcome can be described as reflecting an "informal hierarchy of governance" It reveals a Skandia caught in a web of conflicting forces dominated by those actors that were most able to leverage on these forces: it was a takeover offer driven by US-run investment banks and legal expertise; with UK-inspired takeover rules; and Swedish corporate governance principles, embedded in the Swedish Companies Act. It also featured short-termism among owners, where mainly institutional investor followed a financial rationale and sold off shares for index-tracking reasons rather than operational reasons. In a corporation with a dispersed ownership structure and directors having to comply with shareholder-friendly national legislation this was detrimental to the firm's survival as an independent entity.

As in the Skandia case, the bid by PE funds Apax and Nordica Capital on health-service provider Capio (2006) involved a target with a dispersed shareholder structure. Capio was run with a Swedish shareholder-friendly corporate-governance structure. The bid came to reflect short-termism among institutional investors and regulatory arbitrage, among other things using the Forced Merger Rule (subsequently then abandoned). There was also moral arbitrage as related parties – advisors, directors and the previous Capio CEO – took a number of contradictory positions during the bid process. There were also differences between the two hostile bids on Skandia and Capio. The Capio case targets a much smaller company, the fight was not reported to the general public but remained a story of the financial pages, and the bid fight lasted only two month. At the same time Capio can be analysed in the context of Skandia as many of the actors had the Skandia freshly in mind and used the Skandia case as a role model for their actions. If anything, the Capio fight was a "hyper Skandia".

German truck producer MAN's hostile bid on Scania (2006) sheds light on the challenges facing politicians and regulatory bodies in their work to enhance convergence of corporate law and governance procedures to create an efficient market for corporate control across Europe, while at the same time answering to the financial markets desire for the free movement of capital across Europe. The Scania deal revealed possible misuse of the Directive's mandatory bid rule. Incumbent blockholders could all too easily circumvent it. The nomination committee to suggest new directors on the Scania board was also misused by the largest shareholder VW. The MAN-Scania fight featured a number of cases were institutional investors arbitraged between A and B shares to gain short-term profits. Most decisive for the outcome however, was the ownership of VW, through which a German state both obstructed actors on the capital market from challenging the VW business operations around the millennium and enabled VW to take control of MAN, a conglomerate with an open shareholder structure, and Scania, where the block holder decided to divest its holding. At the same time German labour legislation protected MAN from a Scania takeover. All in all, VW was left as kings-maker, not as a reflection of the work of an efficient market for corporate control, but as a result of personal preferences from one individual brilliantly mastering a highly political and delicate power play (i.e. Dr Piëch).

The three hostile takeovers came to play a role in the 2009 revision of the Swedish Takeover Rules. This spurred the question whether the new 2009 regulation would be more likely to create an efficient market for corporate control than had previously been the case.

Chapter 8

The revised takeover rules 2009

8.1 Purpose and structure of this chapter

This chapter constitutes the sixth and final part of the case studies (Ch. 4). It deals with the amendments to the Swedish Takeover Rules made in 2009. The aim is to determine how and to what extent these amendments addressed the contingencies revealed in takeovers during the sixth takeover wave. The chapter especially focuses on the amendments related to the three case studies of cross-border hostile takeovers Skandia, Capio and Scania. These contingencies can broadly be said to belong to three groups: specific features of the Swedish model of corporate governance, short-termism among institutional investors and possible regulatory and moral arbitrage. All together sixteen amendments were detected half of which can be claimed to relate to problems detected in the three cases. The amendments were mainly focused on facilitating takeover activity on the Swedish market. This was done through clearer rules on how a bid is to be presented to target shareholders as well as by enhancing the shareholder focus of the target board of director. However, the question of the target corporation's role as a value accretive entity was not addressed. To gain a full picture of the amendments this chapter also includes a description of other takeovers that spurred conflicts during the sixth takeover wave.

This study draws on theoretical and empirical material presented through the lens of institutionalism. Following calls by Aguilera and Jackson (2003) and Aguilera et al. (2007) this study proposes to show:

- How (supranational) takeover regulations are adapted to fit into a national context.
- What the effect of these adaptations might be.
- How well these regulations fit into the idea of an efficient market for corporate control in the context of modern finance.

Actors on the Swedish capital market during the sixth takeover wave, 2004–2008, had to conform activity to three sets of takeover regulations – The NBK Takeover rules (2003), the Takeover Directive (2004) and the then anticipated Swedish Takeover Act (LUA, 2006). To this could be added a number of other legal requirements, including the Swedish Companies Act (also Ch. 6.5). The Swedish Securities Council has been granted the mandate to interpret the rules, including "assuring respect for the stock market" (Takeover Rules, 2003, p.1) and that the "rules are applied in light of their purpose, namely to maintain public confidence in the market" (Takeover Rules 2009, I.2, p.7). The study then deals with two groups of revisions of these rules:

- Those done in 2009, dealing with the last NBK Rules ("The Rules concerning Takeover Bids on the Stock Market Nasdaq Omx", Stockholm 1 October, 2009).
- The parallel revisions done through legislation related to LUA and the Swedish Companies Act.

Building on the description of how the Swedish takeover rules have evolved since NBK began to work in 1968 (Ch. 6), the revisions are presented here as the *seventh revision* (also Ch. 6.4 and *Table 8*). An *eight revision* of the takeover rules was carried out in the beginning of 2012 ("The Rules concerning Takeover Bids on the Stock Market NASDAQ OMX Stockholm", 1 July 2012). This last set of amendments can be described as an extension of the work from 2009, in much the same way as the revision of 2003 was carried out in two steps.

The book on Swedish takeover regulation by Stattin (2009) (*Sw:* "Takeovers – Offentliga uppköpserbjudande på aktiemarknaden enligt svensk rätt") – has been used as a tool for understanding the development of the Swedish takeover rules. This includes the description of the amendments between the 2003 version of the Swedish takeover rules and the 2009 version. Stattin (2009) has also been used to increase the depth in understanding the Swedish amendments in relation to the Takeover Directive and the UK Takeover Code. However, whereas Stattin builds on the assumption that efficiency of regulations is seen from a strict shareholder perspective and claims that this should be both sufficient and satisfactory for society, I build on an institutional perspective with a focus on the corporation and its value accretive ability. It is this latter approach (described in Ch. 2) that enables this case study to include a broader set of actors in the efficiency equation, where shareholders eventually take a role as stakeholders among others. This broader focus allows for a simultaneous integration of takeover regulations, corporate law and corporate governance codes in a cross-border hostile takeover process as well as an analysis of these implications for directors on the target board. This can also be used to understand the misalignment between Swedish rules and other European rules.

The rest of the chapter is structured as follows: I begin with an analysis of the Swedish experience of cross-border hostile bids and takeover regulation during the sixth takeover wave (Section 8.2.1). I then argue that the regulatory setting favours the bidding party and as such reflects a takeover market highly conducive to deal making (8.2.2). This is followed by a description of the most important amendments made in 2009 (8.2.3). I summarize the amendments to the NBK 2009 Rules and relate them to takeovers during the sixth takeover wave. In doing so I go beyond the three case studies presented in the dissertation here (8.3). Section 8.4 develops those parts included in the revised rules 2009, which have clearest relevance to the Old Mutual/Skandia and Capio cases. The Skandia case spurred a review of the Insurance Act to align it more closely with the Swedish Companies Act and an update of the Swedish Corporate Governance Code. The Capio deal resulted in limits being placed on activities pursued by investment banks and highlighted the conflicting roles of advisors and directors. This section also addresses amendments that were left out of the NBK regulation and instead dealt with through revised legislation. This includes the Scania deal with possible questionable practises surrounding the Mandatory Bid Rule and by the works of the nomination committee (8.5). As an academic exercise each amendment to the NBK Rules, LUA and Companies Act relevant to the three case studies are analysed as if these amendments had been already in place already during the sixth takeover wave.

8.2 Background of the sixth takeover wave and regulations

8.2.1 Empirical setting

There were a number of takeover fights at the SSE during 2004–2008. The cross-border hostile bids on Skandia, Capio and Scania were only three of the most publicized deals. Other high-profile deals from the same period include Icelandic Milestone's bid on Invik, controlled by investment company Kinnevik, and the fight over bid premia on A shares (Jonnergård and Larsson, 2009), state-controlled France Telecom's preliminary talks with Teliasonera, controlled by the State of Sweden. Other bids that resulted in controversies were the PE bids on health-care company Gambro, Securitas Direct, and there were fights over Finish-Swedish Tietoenator and the Swedish IT-consultant IBS. Yet other bids received much publicity despite not being hostile to the board and management. These include OMX, which was taken over by US stock exchange Nasdaq, and the sale of state owned Swedish liquor producer Wine and Spirits to French owners.

Thus, in the wake of the sixth takeover wave it was apparent that the Swedish takeover market had changed in character. Hostile bids had become more common. It became, if not standard so at least legitimate procedure to launch a bid without a prior recommendation from the board of the target company. The number of cases referred to the self-regulatory body Swedish Securities Council increased at the same time. When the Commerce Stock Exchange Committee, NBK, set out to revise rules in 2003 the number of cases referred to the Securities Council was around 30–35 per year. In 2006 there were 59 cases (AMN, 2006). Many actors on the stock market felt that the NBK revision conducted in 2003 had not sufficiently addressed a number of problems. Thus the actors related to NBK met 2007–2009 to make a seventh revision of the takeover rules. [117]

8.2.2 Theoretical setting

As they worked during the sixth takeover wave, Swedish takeover rules had broadly evolved to meet the needs of three groups of constituents. These groups were; the target management as opposed to the target shareholders; the bidding party as opposed to the incumbent (target) shareholders; and certain shareholder groups of the target company. To meet these needs the Swedish takeover regulation had until 2006 followed three tracks:

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[117] In 2009 the members of the NBK Committee were made up of Chairman Lars Otterbeck, formed CEO of Alecta, and at the time director of Old Mutual; legal advisor Claes Beyer, law firm Mannheimer Swartling; Peggy Bruzelius, CEO of Lancelot and director of Wallenberg dominated companies such as Scania and Electrolux; Johan Bygge, CFO Wallenberg controlled Investor; Björn Franzon, Former Vice President of the Fourth AP fund; Tomas Nicolin, former CEO of Alecta; Marianne Nilsson, head of governance at Swedbank Robur, Anders Nyrén, CEO of Industrivärden, Eva Persson, legal secretary Volvo, Göran Tidström, chief accountant Öhrlings Pricewaterhouse Coopers, Hans Wibom, legal advisor law firm Vinge.

- Imitation of UK regulations, particularly the self-regulatory takeover Code and the Mandatory Bid Rule, ostensibly in an effort to ensure fair and equal treatment of shareholders.
- Acquiescence to EU wishes to limit defensive action by the management and board of the target company, particularly in the Takeover Directive and the Board Neutrality Rule.
- Responsiveness to influential incumbent shareholders to new actors on the modern capital market, both domestic and global, through self-regulatory NBK Takeover Rules and through legislation.

Taken together these tracks appear to have worked to facilitate the success of bids. As such the Swedish takeover regulation during the sixth takeover wave can be described as deal driven, oriented towards the protection of one stakeholder group, the current shareholders of the target corporation and this group's interest of a maximum price. A reinforcing factor in this work was the weak position granted a Swedish board of directors during a hostile bid-process. This preference for deals was enhanced by a number of rulings by the Securities Council that in high-profile cases (such as Skandia, Scania and Capio) allowed activities that had been questioned by some actors on the stock market and contributed to the process of deteriorating public trust in the stock market: i.e. the opposite of the purpose of self-regulation. Sweden, as illustrated in *Figure 13* appeared to develop a two-tier market for corporate control, with one targeting companies with a controlling shareholder (such as Scania with A and B shares) and another one for companies with a dispersed shareholder structure (such as Skandia and Capio).

At the same time directors on Swedish corporate boards had to cope with one regulatory framework, one Companies Act and one self regulatory set up while at the same time having to respond to two different types of shareholder pressure. The role of the directors was complicated further by the expectations set in the Swedish Corporate Governance Code, which included a Swedish adaptation of the UK comply – and – explain framework.

Figure 13. Two-tier Swedish market for corporate control

	Dispersed shareholding	Blockholder control
Friendly		
Hostile	Skandia Capio	Scania

8.2.3 Amendments to the NBK 2009

In March 2009 NBK published its proposal for the seventh revision of the rules for public takeovers on the Swedish Stock Market. These rules were to be adopted by Nasdaq OMX Nordic Stock Exchange, the new name for the Stockholm Stock Exchange and the other list Nordic Growth Market, NGM. The new rules came into effect on October 1, 2009.[118] The recommendations were published in a press release (17 March 2009). It included sixteen amendments to the Takeover Rules (*Table 15* also in *Appendix, Section 5*). The amendments are mainly focused on further aligning the Swedish rules with the UK takeover code. Six of the new recommendations appear to be related to problems that emerged during the Old Mutual bid on Skandia 2005. Three of the amendments appear to be related to the Capio bid in 2006. The question of the Mandatory Bid Rule, related to the Scania case, was originally included in the revision, but it was decided that the issue was to be handled through regulation in LUA instead. The Forced Merger Rule, relevant in

[118] NBK ceased to exist in 2010, after this final revision of the takeover rules. Since then responsibility for the development of Swedish Takeover Rules has rested with the Swedish Corporate Governance Board (Swedish Corporate Governance Board, press release May 18, 2010).

both Skandia and Capio, was addressed in the Companies Act. A last issue targets bid premia and fair treatment of minority shareholders in companies controlled through differentiated voting-rights. This involves Scania but also other cases (e.g. Milestone's bid on Invik).

Here the sixteen amendments have been listed as belonging to four rule groups (*Table 15*). Three rule groups are related to amendments to the takeover rules. These are (1) actions taken by the bidding party, (2) actions taken by the target board and (3) technical issues. A fourth rule group consists of amendments dealt with through legislation and addressed through LUA or the Companies Act. Amendments to the NBK Takeover Rules can be described from many perspectives. If one starts with the level-playing field, issues dealing with the bidding party (rule group 1) and technical matters (rule group 3) both aim at fostering equal treatment of the shareholders in a target company no matter which national stock exchange the stock is traded on (i.e. the principal-principal conflict). Important issues related to this are the assurance of equal treatment of information and the availability of correct and relevant information to determine a "best" or correct market price. In the NBK case this meant aligning the behaviour of actors on the Swedish Stock Exchange with the behaviour of actors governed by the UK Takeover Code, i.e. the listed companies at the London Stock Exchange. Rule group 1 also addresses equal treatment of different share classes.

A second category (rule group 2) addresses the role played by the board of directors of the target company (i.e. the principal-agent conflict). Five of the amendments address directors of the target board, which directors also are subject to a new rule, II.17. The guiding principle appears not to have been to seek further alignment of the Swedish takeover rules to either the UK role model or the EU Directive. Rather, the amendments in rule group 2 seem to express more clearly issues related to the specific Swedish governance model, and the relationship between shareholder owners and directors. In this sense, the revision 2009 of the NBK Takeover Rules led to a divergence from both the Directive and the UK Takeover Code and as a result *lessening* the level playing field.

Table 15. Amendments to the NBK Takeover Rules 2009 (cont.)

Rule 1	Actions by Bidding Party	Example case	Years
II.1	Stricter rules on pre-announcements	France Telecom's bid on Teliasonera was announced in an unclear manner	2008
II.4	More stringent rules for the withdrawal of bids	Old Mutual attempted to make the offer on Skandia conditioned on board acceptance	2005
II.5	Limits on the right to change an already presented offer	During AOL´s bid on Tradedoubler it was unclear if the condition of 90 per cent acceptance might be waived	2007
II.8	Obligations on shareholders following acceptance	In Skandia it was unclear under what condition shareholders could withdraw acceptance	2005
II.11	Equal treatment of different share classes	Milestone's offer to Invik's shareholders included a premium for Kinnevik's A shares over the price of the B shares	2007

Rule 2	Actions by Target Board	Example case	Year
III.3	More stringent requirements for independence when issuing a fairness opinion	When Investor and EQT bid for Gambro, Old Mutual bid for Skandia and Nordic Capital bid for Capio the enrolled investment banks received success fees.	2004-6
II.17	Clarification that the target board shall act only in the interest of the shareholders; neither favouring a certain bidder, nor taking other considerations than price	The Skandia board had difficulty handling diverging interests of shareholder- and stakeholder groups	2005
II.18	Rules handling conflicts of interest within the board of the target company	When private equity firm EQT bid for Q-Med the main owner participated in the bidding consortium	2008
II.19	The target board's obligation to present its opinion on the bid	Should be done when two weeks remain and address all share-classes	
II.20	Clarification of the target company board's obligation to accept a request for a due-diligence	In Skandia the process dragged on and disturbed the daily business of the company	2005

Table 15. (cont.)

Rule 3	Technical Issues	Example case	Year
II.7	More stringent rules regarding the acceptance period	Old Mutual's bid was prolonged a number of times	2005
II.14	Rules limiting rights to make deals outside the public offer	Borsa Dubai's bid on OMX included a partial offer with a price guarantee	2006
II.15	The right for an unsuccessful bidder to buy new shares reduced from 9 to 6 month	General adaptation to the UK takeover rules	
II.24	Limits for bidder to return with a new bid to 12 month	General adaptation to the UK takeover rules	

Group 4	Changes not addressed in the new takeover rules	Example case	Year
	Statutory Merger (ABL, 2009)	New law for statutory mergers implemented 2008: VLT, Skandia, Capio	2004-6
	A new level for mandatory bid be implemented at 50 % (Swedish takeover directive according to LUA)	VW acquired the Wallenberg Group's shares in Scania. In March 2008 this gave control of 37.7 % of capital (68.6 % of votes) without having to bid for all shares. Still not changed	2005-8

NBK (2009); Nachemson-Ekwall, Dagens Industri (2009)

There is also a fourth group of amendments triggered by market activities during the sixth takeover wave in Sweden. These are issues relating to legislation, the pricing mechanism and distribution of power between the bidding party and target shareholders. These are the Forced Merger Rule, which was revised substantially and the Mandatory Bid Rule, which despite much discussion was not addressed. The FMR relates to the Swedish Companies Act and its regulation of statutory merger whereas the MBR is dealt with in LUA as part of the Swedish Takeover Directive and not the NBK Takeover rules.

8.3 The general role of directors: II.17

Many of the amendments to the NBK Takeover Rules 2009 address issues related to the role of the board of directors of the target company. The purpose of the new rule II.17 and the revision of the 2003 rule II.19 appears to have been to clarify the role of the board as serving the interest of the (current) shareholders and no other stakeholder group. In doing so the revised Swedish Takeover Rules differ from the EU Takeover Directive Article 3, dealing with the General Principles and Article 9, dealing with the obligations of the target board, including the Board Neutrality Rule. The new rule II.17 and the revised II.19 also diverge from the UK Takeover Code. To fully understand this change this section first presents a comparison between relevant parts of the Swedish Companies Act, takeover regulation and the EU Directive. Then the section moves on to a discussion of the Swedish shareholder-friendly approach in comparison to other European countries, including Britain, Germany and the Nordic neighbours.

As a start, the new rule II.17 says: ”The board of the target company shall in relation to the offer act in the interest of the shareholders.” This relates to the revised rule II.19 dealing with the target board's obligation to present its opinion on the bid:

> “The board (of the target company) shall in relation to what the bidder states in the press release or offer document present its opinion on the takeover's implication for the company, especially as regards issues relating to employment, and its opinion on the bidder's strategic plan for the target company and the effects it can be expected to have on employment and the sites were the company have operations.”

According to Stattin (2009) the formulations in the Takeover Directive, dealing with the General Principles, Article 3:1, differ from NBK (2009) rules II.17 and II.19. Stattin claims that the formulations (below) in the General Principles Article 3:1 are unclear:

> 1(b) The holders of the securities of an offeree company must have sufficient time and information to enable them to reach a properly informed decision on the bid; where it advises the holders of securities, the board of the offeree company must give its views on the effects of implementation of the bid on employment, conditions of employment and the locations of the company's places of business;
>
> 1(c) The board of an offeree company must act in the interests of the company as a whole and must not deny the holders of securities the opportunity to decide on the merits of the bid.

The implication of the decision by NBK both to include a new rule section II.17 and to revise section II.19 in NBK 2009 is best understood through the interplay between the role of directors in the Swedish companies act and the development of capital market law. These regulations have contradicting goals in some respects, which become present during a contest for control (Stattin, 2009). As will be shown below the revision in II.19 addresses a fundamental conflict between takeover rules and Swedish corporate law. A detailed discussion of II.19 is found in section 8.4.

To recapitulate, according to the Swedish Companies Act the primary stakeholder group in a limited company is the shareholders.[119] The limited company works with a hypothetical and common interest, objectively stated, since no one can know what individual shareholders wish apart from what has been decided on by the general meeting (Taxell, 1961; Stattin, 2009, pp. 64–65). Judged objectively the company's interest will be close to generating profit, but is likely to be more complex. Profit is in itself a complex purpose. Corporate law offers no guidance on the size of this profit, how it is to be generated or within what time span. In short, corporate law does not differentiate between short and long-term investment horizons. As explained in Stattin (2009), capital market law differs in certain respects from company law. Capital market law not only accounts for shareholders and minority shareholders, it also looks

[119] Even in stakeholder regimes it is widely accepted that the shareholders are the primary stakeholder group with special rights to act through the AGM.

after the interest of investors in general, which means shareholders that have not yet become investors, and in some ways also shareholders that have been investors (Stattin, p. 64). The basic purpose of capital market law is to ensure that the public information given is such as to ensure that the markets valuation as reflected in the pricing of the company's shares is as "correct" as possible (Stattin, p. 65).

Takeover rules differ from both corporate law and capital market law. In a takeover situation the directors of the target company act in a legal context where they do not have the primary role – rather they act as a substitute and representatives or fiduciaries for the company's stakeholders. At the same time the legal framework surrounding takeovers has been based on the idea that the company shall not be viewed as an independent interest, as the shareholder's right to sell cannot be violated. This view is consistent with both British and Swedish practice as well as the general principles of the EU Takeover Directive. As previously described the US has a different approach, as does Germany with its stakeholder view.[120]

Emanating from a strict shareholder-value model of corporate governance, takeover rules inevitably evoke the idea of perfect capital markets. This shareholder-rights focus make takeover rules easier to deal with from a legal perspective than they would be if different stakeholder interests were also included. As mentioned in previous chapters a focus on the shareholder-value model guided the European Commission in its work with the 13th Takeover Directive but this was not wholly successful. The Directive is also full of political compromises with Article 9, dealing with the duties of the board of directors, and Article 11, dealing with the break-through rule, both being opt-in and opt-out clauses (see Ch. 3.3.2).

As mentioned above, Stattin (2009) highlights what are from Swedish legal perspective, "unclear" formulations in the Directive's, General Principles Article 3. The principles are presented in the introduction of the 2009 revised NBK Takeover Rules which begin by stating that the

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[120] The idea of shareholder supremacy has in the post-financial crisis era become heavily debated in Europe. This includes the UK where the directors' passivity during a takeover is questioned in the Kay Review (February, 2012).

takeover rules are built on the Directive, which can be used as a guide in situations where the new rule II.17 and the revised rule II.19 either do not give appropriate answers or in cases where the NBK Takeover Rules do not apply. The complication between the NBK 2009 and the EU Takeover Directive concerns the unclear mentioning in the General Principles of ”employees” (Article 3:1 (b)) and ”company as a whole” (Article 3:1 (c)). These issues are also addressed further in the Directive Article 6:1, where it is stated that the board of the target company must make public a document setting out its opinion of the bid and the reasons on which it is based, including its views on the effects of the implementation of the bid on all the company's interests, specifically employment, and on the bidder's strategic plans for the company and their likely repercussions on employment and the locations of the company's places of business as set out in the offer document.

According to Stattin the writing of the Directive Article 6:1 reflects an unsolved stakeholder issue, which must be understood in a national context. In UK and US capital markets law, the directors' fiduciary duties in relation to the company and its shareholders are more clearly described than in the Swedish Companies Act, with its collective and more hypothetical shareholder interest.[121] The UK Takeover Code uses the same wording of the ”company as a whole” principle as in the EU Takeover Directive. Notably, British minority rights are rather weak and the Continental European meaning of stakeholder includes more parties (Stattin, 2009, pp. 66–69). The initial work with the Takeover Directive in 1997 actually included intentions for the board of directors to act in all the interests of the company, including the employees. This was later changed. In German company law the emphasis rests on the social role of corporate activity, and pursuing profits for shareholders is secondary

[121] An example of this is the US management revolt to the hostile takeover raids of the 1980s, after which many companies choose to reincorporate in Delaware, a state with a well-developed body of case law system which better take cares of the interests of the company than in other states, including allowing for the management-led board to engage into frustration measures to obstruct a hostile bidder without clearance by the shareholders.

(see section 5.6, addressing the German company law and section 6.7, addressing German takeover regulation).

Swedish and Nordic corporate law appears to be more aligned with the British shareholder perspective while at the same time offering fairly strong minority-rights protection. But Swedish takeover regulations have never addressed the stakeholder issue. In the Swedish takeover rules, the NBK 2003, stakeholders were not even mentioned. This means that the directors appear to have been offered a certain amount of ”freedom” in their interpretation of how to act on the “company as a whole” issue. Paragraph II.14 in the takeover rules from 2003 states that the board shall act in the interest of all shareholders. The board must neither favour a certain shareholder or group of shareholders, nor take its own position as directors into account. NBK 2003, II.14 does not include the word “company”, which is present in both the UK Takeover Code and the Directive. NBK 2003 stated that the directors should give their opinion on the bid, but gave no guidance on to the level of detail to include. Nor does LUA 2006 include any new reference to the opinion by the board of directors. It only mentions that employees should be “properly informed” about the bid (LUA, Ch. 4; Information to employees).

Thus it seems that Sweden had, at the time of the implementation of LUA 2006, opted for a position whereby it is the shareholders' interest that is the strongest. This stance can thus be concluded to merely have been enhanced with the board neutrality rule in the Directive (Article 9:2)[122], Notably, the BNR is an opt-out rule. This means that nations without it can include more of a stakeholder perspective when taking defensive actions (Germany and Denmark are examples).

Despite this apparent ”shareholder focus” of Swedish takeover rules, both the EU Takeover Directive Article 3:1(c), and the NBK Takeover Rules 2003 brought complications to the Swedish context. The Directive's Article 3:1(c), does not offer guidance in a number of other specific situations. It abstains from dealing with the possible conflicting (political) ambition to construct an efficient takeover market, which both

[122] The BNR states that the board of directors may not take frustration actions without prior clearance by the general meeting.

enables frictionless cross-border hostile takeovers and assures a fair treatment of minority shareholders. It neither deals with the board's obligations related to due diligence (discussed in Ch. 7.6).

To correct this lack of clarity the 2009 revision of the Swedish Takeover Rules complemented the Directive's Article 3:1(c) and the 2003 NBK II.14 with a new rule II.17. As stated previously in this section this rule states that the board of the target company shall in relation to the offer act in the interest of the shareholders. Thus, since 2009 there is no doubt that the board of directors of a Swedish company has its fiduciary obligation to the shareholders where the stakeholder interest is reduced to a mere information memorandum, such as information related to possible redundancies for employees or the movement of production sites.

Denmark, Norway and Finland, Nordic countries with great communality in the corporate law, have however not followed the Swedish development of the clear shareholder focus of the takeover rules. The Finish Takeover Rules address the director's general obligation to act in the interest of the company and the shareholders (Finish Companies Act, ABL 6 Ch. 2 §). This includes acting in accordance with the company's objective to generate profit for shareholders if nothing else is stated (ABL 1 Ch. 5 §). This view, which is close to what is written in the Swedish Companies Act but not in the NBK 2009 Rules, allows for director's of Finish companies to guard the company as a wealth-accretive entity for its shareholders long-term, rather than in relation to the current market value of other stocks. Norway, not being a EU member, has not implemented the Takeover Directive but otherwise follows part of its intentions. The Norwegian Code of Corporate Governance and Takeovers (13), states: "The board of directors should not seek to hinder or obstruct takeover bids for the companies' activities or shares unless there are particular reasons for this…"(Norwegian Code of Corporate Governance and Takeovers, 2004). The Danish Takeover Rules (2007) do not differ from the EU takeover rules in this aspect. Denmark has also chosen to opt-out on the board neutrality rule.

The Nordic countries also differ in their formulation of governance codes and this has had implication for their approach to takeover regulation. There are for example differences as regards to the length of directors' terms on boards. In Norway directors are voted in for two-year terms, in Denmark directors are voted in for three-year terms and it is recommended in the Danish Corporate Governance Code that the terms overlap. In both Finland and Denmark the nomination committees are organs within the board. Norway has an external nomination committee, made up of at least one fully independent director and is elected at the AGM.

8.4 Statement of the board: II.19

This section deals more specifically with the 2009 amendment to the NBK Takeover Rules related to the board's statement on the bid, the revision of II.19, and its more shareholder-friendly formulation than in previous versions. A comparison with the formulation in both the Directive and the UK Takeover Code is included. The section ends with a retrospective analysis of the Skandia and Scania cases.

During a takeover the opinion of the board is generally deemed very important as an aid for shareholders in decision-making. However, the level of information regulations required differs between the Directive and the NBK rules, both those of 2003 and the revised version 2009. The Takeover Directive Article 8.5, dealing with disclosures state:

> ”The board of the offeree company shall draw up and make public a document setting out its opinion of the bid and the reasons on which it is based, including its views on the effects of implementation of the bid on all the company's interests and specifically employment, and on the offeror's strategic plans for the offeree company and their likely repercussions on employment and the locations of the company's places of business as set out in the offer document.”

The exact same wording also appears in the UK Takeover Code rule 25.1. In NBK 2003 the role of the target board is, as mentioned previously, in line with the traditional Swedish shareholder focus. NBK section II.14 did not offer any guidance of specific details to be expressed. NBK II.14 stated that the board of directors shall present its view on the bid, and reason for it, at a time that gives shareholders sufficient time to decide on which action to take. It is specified that the board should act in the interest of all shareholders: ”This means that the board might not in its decision be governed by the interest of a specific or group of shareholders and not by the board's own position”, (NBK 2003, II.14). However, in the revision 2009 the opinion of the board is specified both in more detail, and diverges from the EU Directive and the UK Takeover Code. As mentioned previously (section 8.3), NBK II.19 states that the board of the offeree company, the target, has to present an opinion on the bid no later than two weeks before the bid expires. Added to this, however, the revised II.19 specifically limits the duty of the target board to (italics added): "Commenting on information which has been presented in the *press release* by the offeror or the offeror's strategic plans for the target company, especially as regards to employment and working sites." Thus NBK 2009, II.19 gives the target board a clear signal to set no other priorities than to maximize the present economic value of the bid. This wording strengthens the role of the Swedish board as a passive agent of the shareholders during a takeover. The board's role becomes limited to relating to a bidder's comments in a press release and searching for the highest bid available, i.e. current share price. As a result NBK 2009 is much more shareholder focused than both the EU Directive and the UK Takeover Code (but it does not forbid the board to present more information).

In a retrospective analysis of Old Mutual's bid on Skandia this means that the conflicting views of the Skandia board, which included the three views – long-term shareholder value, short-term shareholder value and stakeholder value, were resolved in favour of current (short-term) shareholder value. It also means that the Scania CEO Östling's talk to a group of incumbent shareholders of Scania about prospects for long-term corporate value creation can be described as reflecting a conflict between the Östling/Scania management stakeholder view and the markets wish for a short-term price discussion.

NBK section II.19 require the board to offer an opinion no later than two weeks before an offer expires, but this timeframe does not address the information needs of shareholders, especially index-tracking institutional investors who often simply sell before the board acts. The timespan does not take into consideration the different interest of incumbent shareholders and hedge funds, as many incumbent index-driven institutional investors might feel obliged to trade in the share ahead of a board recommendation. This means that a board, with a mandate that can expire at anytime (ten per cent of the shareholders in a Swedish company can call an EGM and suggest new directors), with a focus on the interest of current shareholders, will easily be pressed to take a short-term (current) view on the value of the bid, setting the long-term prospects of the company aside. In a retrospective analysis this dilemma of board passivity showed up in all three cases Skandia, Scania and Capio, being especially important for the outcome of Skandia where a new group of institutional investors working through the nomination committee challenged the view of the incumbent board of directors. In NBK 2009 (current) shareholder power in relation to incumbent directors appears to have been further enhanced.

Swedish takeover rules guide directors toward a clear shareholder focus when valuating a bid. This contrasts with the writing in the revised UK Takeover Code. The UK Takeover Panel Code Committee acted in the wake of US Kraft's cross-border hostile takeover of UK Cadbury and the resulting factory closures. [123] In a revision of 2010 it suggested amendments to the Code in favour of *strengthening* the position of other stakeholders than the shareholders. Addressing hostile takeovers and

[123] In December 2009 Financial Times wrote that Lord Mandelson, Britain's Business and Enterprise Secretary, had warned the board and management of Kraft and was quoted saying: "If you think that you can come here and make a fast buck you will find that you face huge opposition from the local population . . . and from the British government." (Guthrie & Wiggins, FT, 12 May 2009). The UK secretary's comment was unprecedented, marking a government intervention previously unheard of in a country where politicians tend to steer clear of becoming involved in take-over bids unless there are serious competition concerns. In the UK House of Commons in March 2010 there were calls for a "Cadbury Law to prevent hostile takeovers of British companies which are not in the public interest" (Wiggings, FT, 12 March 2010).

short-termism, the *tenth version* of the UK Takeover Code says (rule 25.2) that the board of the target company shall include its opinion on the bidder's strategic plans for the company, the bidder's effect on all the company's interest and especially its locations and its employees:

> "The provisions of the Code do not limit the factors that the board of the offeree company may take into account in giving its opinion on the offer in accordance with Rule 25.2(a). In particular, when giving its opinion, the board of the offeree company is not required by the Code to consider the offer price as the determining factor and is not precluded by the Code from taking into account any other factors which it considers relevant."[124]

8.5 The role of directors during the preparation of a bid

The amendments to the NBK Takeover Rules 2009 address two issues related to the director's role in the preparatory phase, the *pre-announcement phase*, of the bid: due diligence and different deal-protective devices. These issues are addressed in the UK Takeover Code but not in the EU Takeover Directive (here Section 8.5.1 below). The other issue addresses *conflicts of interest* among groups of shareholders and among directors, NBK rule II.18. This rule can be interpreted as a Swedish version of the concept of *concert parties*, dealt with in the UK Takeover Code and the EU Takeover Directive (here Section 8.5.2).

To enhance takeover activities across Europe the pre-announcement phase of a bid process has received much attention. Despite it being possible to present a bid directly to shareholders in a listed company at the SSE without previous consultation with either shareholder groups or the board and management, this is seldom seen as a

[124] The Panel on Takeovers and Mergers, 19 September, 2011. Ch. 25 § 2:1, p. J18

viable option for the bidder.[125] Very few bids are ”truly” hostile in this sense, as they are quite costly and complicated compared to a friendly bid (Gilson, 2005). Rather, standard procedure appears to be for representatives of the bidding party to make initial contact with the board or management to find out if a bid might receive a positive board recommendation.[126] A friendly approach is then usually followed by a written indicative bid and a subsequent request for pursuing due diligence and entering into different deal-protective measures. This means that the board's role during a pre-announcement phase might be of great importance for the outcome of the bid when it is presented to the shareholders at a later stage.

8.5.1 Due diligence: II.20

Before the sixth takeover wave both due diligence and deal protective measures were viewed as unusual procedures in takeovers involving continental European listed companies. The due diligence is not addressed in the UK Takeover Code. However, the Code deals extensively with different forms of deal protective measures, which indirectly addresses the right to conduct a due diligence too. In this section the issue concerning due diligence is discussed with a special focus on the Old-Mutual Skandia case.

The question of due diligence forces the board to evaluate its strategic plans for the company going forward. At the same time the due diligence highlights a dilemma related to Swedish board of directors, as both being suggested to the board by individual shareholder groups and being obliged by the Companies Act to act in the interest of all shareholders

[125] There are no known cases during the 6th takeover wave in Sweden and most likely not in any other countries either. However, it does happen that a competing offer is brought forth in public without consultation with the board of the offeree company, but then the company is already ”in play”.

[126] It is another issue that the meaning of hostile bid is supposedly hostile to the board and management in an Anglo-US context whereas addressing a bid directly to the shareholders circumvent the issue of hostility altogether.

alike. The issue of due diligence relates to two branches of law – company law and capital markets law. In relation to company law allowing a due diligence might conflict with the directors duty of care. Accordingly the board is obliged to assure that a due diligence is carried out with care, that as little information as possible is given and that the time is limited as not to hamper the company's business.

The capital market law and shareholders' interest was dealt with in NBK 2003, stating that: "The board of the target company shall participate only if the board believes the indicated bid to be of interest for the shareholders…and deemed a necessity for the bid to be presented." (NBK, 2003; II.15). To this can be added that any confidential information given must be made public before the bid is finalized, that the bidder is prevented from trading in the stock before the information is made public and that the bidder has to sign a confidentiality agreement and ask for the due diligence process in writing. In the amendments of the takeover rules 2009 it was added that: "The board should also endeavour to ensure that the investigation is conducted as quickly as possible in order to avoid unnecessary disruptions to the offeree company's business." (NBK 2009; II.20)

The board's right *to allow* a due diligence, with care, seems thus to have been addressed. The difficulty arises when the opposite question is brought forth, in the case of director's right *to deny* a due diligence. In the Swedish Companies Act that is not a problem, as company law clearly states that it is the director's duty to act with the best interest of the company. According to the Companies Act there is no obligation for directors to comply with a wish from a group of shareholders or an external party to be allowed to conduct a due diligence.[127] Nor is it stated that the directors shall use the development of the e.g. stock-price for guidance. From the perspective of the Companies Act the delicate issues related to the work of a due diligence are addressed - such as risks connected with hindering the company from pursuing its ordinary business activity, risk

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[127] Rather, shareholders are free to suggest that directors are removed at an EGM, which they can call if they have more than 10 per cent of the votes.

connecting with putting the company ”in play” and risk of breach of confidentiality.

However, in capital market law, directors have the duty to allow a due diligence if it can be perceived to be in the interest of the shareholders getting the highest possible market value for the company. In the statement from the Swedish Shareholders Council, AMN 2006:55, it is left to the board itself to decide on the due diligence. The issue was not dealt with in the amendments to the NBK Takeover Rules of 2009. Stattin (2009) argues that it is difficult to foresee a legal case that tests the directors' obligation to allow a due diligence to be conducted.

In the Old Mutual-Skandia case the due diligence issue was an important factor in the bid process. In May 2005, after the letter with the indicative bid had leaked out and the Skandia-share had risen on the stock market, the board of Skandia was confronted with three dilemmas: it had to choose between allowing or denying a due diligence, it had to choose between acting for the shareholders as a group or in the interest of the vocal director, Cevian's Gardell, who perceived it to be in the interest of the shareholders that a due diligence was pursued. Finally, the board had to handle the timing and level of detail in the actual dd-process. In the Skandia case the dd-process ended up lasting over two month and occupied the top management team at the period.

In a retrospective analysis I would claim that the 2009 revision of the NBK Takeover Rules handled the problem with the length and time-consuming due diligence issue in Skandia, but the revision did not offer the board guidance in relation to allowing a due diligence in the first place. NBK has not taken into consideration that a due diligence process might be an important aspect of the actual bid process of a Swedish company, as allowing it can be an important step towards putting a company in play (i.e. a bid process becomes unstoppable and there will be some sort of deal no matter what). In the Old Mutual-Skandia case part of Old Mutual's initial contacts with the Skandia board included a wish to bring forth a *friendly* bid. That did influence the board's willingness to cooperate. A similar experience was made by Swedish fashion-clothing brand Gant after Swiss Mais Freres had taken initial amicable contacts with the Gant board of director, recapitulated in the story of

Gant (*Sw:* ”Gant: När Tre Svenska Entreprenörer Gjorde ett Amerikanskt Varumärke Globalt”, Björk, 2008). Mais Freres later presented a hostile bid that succeeded.

8.5.2 Conflict of interests: II.18

The Swedish Takeover Rules do not include the notion of “persons acting in concert”, used in both the UK Takeover Code and the EU Takeover Directive. The NBK rules have instead settled for a discussion concerning “conflict of interests”. This follows different views of shareholders that in British governance are an “uninformed group” whereas the Swedish governance model presupposes the presence of a large shareholder/s that is/are both informed and active on the board. Here the different meanings between “acting in concert” and “conflict of interests” are first developed in detail, including a description of what this implies for the Swedish takeover regulation. The analysis reveals that the issue of regulatory and moral arbitrage connected with joint activities between related parties during bids in the sixth takeover wave were not fully addressed in the revision 2009. The section ends with a retrospective analysis of three cases Skandia, Capio and Scania, including a special focus on the Capio-case.

In the EU Takeover Directive and the UK Takeover Code the issue of acting in concert is not limited to the actual bid situation but addresses the whole issue of people acting with a common agenda. Article 2.1 (d) in the Takeover Directive (2004):

> ”Persons acting in concert” shall mean natural or legal persons who cooperate with the offeror or the offeree company on the basis of an agreement, either express or tacit, either oral or written, aimed either at acquiring control of the offeree company or at frustrating the successful outcome of a bid. (p.15)

The UK Takeover Code is even more specific in its definition of acting in concert. It mentions different actors such as advisors, fund managers and legal experts. The Code Article 9:6 defines persons acting in concert as any ”directors of a company which is subject to an offer or where the directors have *reason to believe* a bid is imminent”. Thus in the UK Takeover Code a director who at an early stage is working together with a bidder – i.e. he or she has reason to believe there will come a bid – is seen as related to the bidder. The question of “concert party”, related to shareholder activism, is further addressed in the UK Combined Code. Co-operations between different shareholder activists can lead to them being seen as concert parties if an agreement includes ”board-control seeking” resolutions.

The Swedish regulation has abstained from using the concept and term concert party. NBK 2003 refers to persons with “conflicts of interest” and in the 2009 version the discussion revolves around “measures taken by parties closely related to the offeror”. The differences emanate from the Swedish ownership governance model, with shareholders both present on the board and on the nomination committee as representatives of the largest shareholders. On the Swedish capital market conflicts of interests among different shareholder groups — the minority shareholders and the controlling blockholder — are constantly present and expected to be dealt with on an on-going manner. In the Swedish context the conflict of interest also exists in companies with a dispersed shareholder structure, as the shareholder influence in such a firm will be shared between the largest actors among the small shareholders, often an institutional investor of some kind. Here too, this “conflict of interests” is dealt with on an on going basis, for example by restricting insider information shared by the chairman of the board to members of the nomination committee. From a capital market law perspective the Swedish owner-governance conflict can thus be split into three groups – shareholders with board representation, shareholders without board representation and potential (future) shareholders.

In NBK 2003 the role of directors that co-operate with a bidder during the preparatory phase was not addressed at all. However, the director’s fiduciary duty was addressed in relation to frustration actions. The NBK 2003 rule II.16 stipulated that a director might not act if he or she had reasons to believe that a ”seriously meant bid” was in preparation, or a bid had been received in writing. However, the Directive’s or

Takeover Code's question of knowledge being ”expressed” or ”tacit” are not addressed (Article 2.1(d); above).

In some situations the Swedish definition of “conflict of interest” appears to be clearer than “concert party”. This relates for example to activities such as related party transactions, tunnelling or rent seeking by management or controlling shareholders. Cases includes situations were a director of a target company or part of management is involved in a buy-out offer or a bid on a subsidiary. However, these cases are not handled in NBK 2003 but dealt with separately through listing requirements of the Stockholm OMX stock exchange.[128]

NBK 2003 defined a person related to the bid as a person that has just had an executive position as part of the management or as board member. The length of time passed in the mentioning of ”just” was not specified, but should, according to the comments in NBK 2003, be understood in relation to the goal, which is to narrow the knowledge gap between different shareholder groups. To level this information gap the board was also obliged to present an opinion from an independent advisor.

Sweden addresses the question of ”acting in concert” for the first time in LUA 2006. However, the LUA definition also differs from both the EU Directive and the UK Takeover Code. In some ways the Swedish definition of a related party is clearer than the definitions in the EU Directive and the UK Takeover Code. LUA Article 5.3 states that: ”someone who cooperates with a bidder with the aim of gaining control” and ”someone who cooperates with a bidder to facilitate the success of the bid” is acting in concert with the bidder. As a result the definition in LUA 2006 appears to go further than NBK 2003.

The term concert party is not included in NBK 2009. Still NBK 2009 offers a more detailed description of a related party than in NBK 2003. This is addressed in NBK 2009, II.18, stating that:

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[128] This is discussed in the Leo Law (*Sw:* “Lagen 1987:464 om vissa riktade emissioner i aktiemarknadsbolag, m.m.”) and also addressed in the Swedish Companies Act (Ch.16).

> "A director of a target company many not deal with preparatory matters related to a bid if the board member, as a result of common interest with the bidding party or of other reasons, might have interests opposing the shareholders' interest. This also applies for the CEO." (p. 40)

The tricky question in the revised NBK Takeover Rules of 2009 is to decide where to draw the line between general talk of a deal with a director, or the actual knowledge by a director of an upcoming bid in the Directive's wording of ”tacit” or ”actual” knowledge. For a board representative backed by a controlling shareholder the issue is delicate as it is both common for a bidder to approach the controlling shareholder in advance and for a controlling shareholder to itself initiate a sales process, i.e. putting the company "in play". This also sheds light on the question of the signing of irrevocable agreements with large shareholders, addressed in the UK Takeover Code but not mentioned in either the EU Takeover Directive or the NBK Takeover Rules of either 2003 or 2009. Neither NBK 2003 nor 2009 address the issue of ”board-control seeking” resolutions either. This implies that institutional investors can at the same time engage themselves both in the works of the nomination committee to suggest directors and act in support of a bidder.

The issue of directors' knowledge is addressed in the Swedish Companies Act. If a director has knowledge of certain facts pertaining to the company's capital situation (i.e. that the company suffers from a certain capital deficit), this knowledge will probably be attributed to other board members and the CEO, who are then presumed to have the same knowledge. If the person that actually knows something refrains from informing the other directors about such facts, it might be deemed a breach of contract of duty and lead to liability for damages (Stattin, 2009).[129]

[129] Stattin (2009) interprets the section in the Companies Act 25 (Ch. 18 §2: *Sw:* "Om vetskap existerar hos en organledamot, skall bolagets styrelse och verkställande direktör anses ha vetskap. Om den som faktiskt vet något underlåter att meddela detta kan det föranleda skadeståndsskyldighet").

LUA defines knowledge as ”having well founded reason to believe” (LUA; 5 Ch.1 § (*Sw:* ”grundad anledning att anta”). LUA thus goes further than the Takeover Directive, which requires “actual” knowledge while at the same time settles for less than the UK Takeover Code, for which it is enough that a director has ”reasons to believe”. NBK 2009 rule II.18 addresses this when writing that:

> ”It is not possible to provide an exhaustive list of circumstances constituting such a conflict of interest as referred to in the provision. This must be determined in each individual case taking into account, for example, the nature and scope of the director’s connection to the offeror, undertakings relating to board duties, etc. The rules must also be applied in light of their purpose, namely to maintain public confidence in the market...” (English translation by Nasdaq OMX Stockholm, 2011; p. 41)

During the sixth takeover wave in Sweden there were a number of cases where the question of related parties had implication for the takeover process. This includes the whole array of director’s responsibility, the transformation for individual board members from a role of independence to a role of actually acting in concert with a bidding party. The question was present in different ways in all three hostile bids: Skandia, Capio and Scania.

In Skandia, director Gardell was CEO of Cevian, active in enticing Old Mutual to bring forth a bid, participated in the board’s preparations related to the bid, and also signed an irrevocable commitment with Old Mutual. Gardell also had contacts with other shareholder groups, including the large investor Fidelity. Also in Skandia a representative of the activist fund Paulson & Co became chairman of the nomination committee while at the same time supporting the Old Mutual bid.

In the preparatory period of the Capio bid the question of concert parties and knowledge by parties with vested interest in a possible deal was apparent particularly in the different positions held by Capio chairman Holtback and the previous Capio CEO Båtelson.

In retrospect the *acting-in-concert* question and knowledge, “tacit” or “actual”, could have been addressed at the time of the MAN-bid on Scania. In 2006 the Scania board included three directors related to Volkswagen, including chairman Pischetsrieder. The Scania board also included two directors directly related to the Wallenbergs, one who also held a directorship at Investor and Wallenberg Jr., a director in the Wallenberg funds. The two "independent" directors also held directorships of two Wallenberg-controlled companies, Atlas Copco (i.e. Staffan Bohman) and Electrolux (i.e. Peggy Bruzelius). Personal relations were further strengthened by cross directorships in a number of Wallenberg companies.[130]

The VW CEO, also chairman of Scania, and MAN's chairman held discussions concerning a possible deal between Scania and MAN in the spring of 2006. The actions taken by the directors on the Scania board after the bid was presented in public might also be addressed. The Scania board addressed the MAN offer in five public statements in the autumn of 2006. Only in one statement, of October 12, did the representatives of VW abstain from participating in the board statement, due to conflict of interests. In all other statements the board unanimously recommended Scania shareholders to reject the bid. The tacit issue mighty also have been addressed in light of Volkswagen's share purchase in MAN, enhanced investment in Scania shares and in the purchase of the holdings by Investor and the Wallenberg funds.

The questions of related-party and concert-party, ”tacit” or ”actual”, do not lend themselves to easy discussions of hypothetical outcome in retrospect.[131] NBK 2009 takes care of some of the issues, related to previous management, and it can thus be assumed that this could have had implication for the Capio deal. However, NBK 2009 gives less guidance with regard to directors.

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[130] Scania annual report 2006, and in line with the definition of independent directors in the Swedish Corporate Governance Code.
[131] A study of the nature of knowledge goes beyond this dissertation.

8.5.3 Concert parties, "tacit" and MAN-VW-Scania

Official Swedish bodies appear not to be fully coordinated in their approach to takeover regulation. An example of this is the usage of the word *tacit* during the MAN and Scania process. The Swedish Financial Authority and the self-regulatory body of the Securities Council hold opposing views. This is illustrated in a detailed description of the triggers of MBR rule in Scania (also discussed in section 8.8). Following the VW share increase in Scania in 2008, SFSA decided to open an investigation related to the Mandatory Bid Rule and related part transactions. The purpose was not to overrule the self-regulatory body of the Securities Council, but to clarify possible uncertainties.[132] SFSA focused on the fact that uncertainty had arisen on the stock market due to the issue of whether an acting-in-concert relationship existed between VW and MAN, which would have obliged MAN to launch a mandatory bid.[133] SFSA looked into whether MAN could be obligated to launch a bid with reference to its relationship to VW or whether MAN had to take into account VW's ownership as well.

The investigation by SFSA offers a perspective on the Swedish Takeover-rules related to "concert parties". Market participants can be considered to be acting in concert in different ways. Relevant in the VW–MAN–Scania case is LUA 3 Ch.5 § 5 section, which states that an acting-in-concert relationship arises between two market participants if they cooperate for the purpose of attaining control over a firm, in this case, Scania. The difficulty arises in the definition of "concert party". LUA has, as mentioned previously, settled for a definition that deviates from both the EU Takeover Directive and the UK Takeover Code. The provision in LUA refers to the parties as "co-operating" in the sense that it refers to "a written or oral agreement to cooperate" (prop. 2005/06:140, p. 106).

SFSA noted that in the EU Takeover Directive Article 2:1, which

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[132] There was a public hearing in parliament.

[133] SFSA, 10 April 2008, "Decision regarding a possible mandatory bid in Scania AB, FI Reg. no. 08-3068

deals with definitions and to which the preparatory work of LUA refers to as well, it is stated in point d), that it is a question of cooperation; “On the basis of an agreement, either express or *tacit* (FI’s italics), either oral or written”. SFSA questioned the exclusion of “tacit” in LUA, writing in its investigation:

> “There is no equivalent definition adopted in Swedish legislation. Nor is it apparent in the preparatory work why the legislators do not mention the directive’s reference to tacit agreements. It is FI’s position, though, that the law should be interpreted in a way that is in line with EU law and that such cooperations contemplated in chapter 3, section 5, point 5 of LUA also cover tacit agreements between two parties.” (SFSA 08-3068, p.3)

In parallel with the UK Takeover Code, this SFSA definition of tacit does not require an agreement to form a voting trust or coordinated conduct of a specific type. The UK Takeover Code also simply presumes that a ‘concert action’ exists in the absence of contrary evidence. The SFSA view is supported by Stattin (2010), who points to the lack of explanation of why LUA abstained from including tacit agreements. VW had directors on the MAN board since the spring AGM of 2007.

SFSA also takes the point further, stating that it is ”furthermore clear that the cooperation is intended to acquire control of a company” SFSA also states that everytime a new share purchase is made there is a need for a new exemption to be granted to the MBR and that this also goes for the acting-in-concert issue. Thus in the investigation, SFSA found existing circumstances supporting a belief that MAN and VW were acting in concert, and that MAN, through its share acquisitions and the VW purchases in the spring of 2007 and winter of 2008, ought to be obligated to launch a mandatory bid.

The next question to address was which party was to be obliged to make the bid, the party that had triggered the purchase or any other party? Since it was VW that triggered the share purchase it seemed logical to oblige VW to make the mandatory bid.

Despite these arguments, SFSA ruled that VW ought to be granted an exemption. Since VW was previously granted an exemption by the

Swedish Securities Association, this implied that VW would not be obligated to make any bid on the remaining shares in Scania. In its decision, SFSA noted that no one had made an appeal to SFSA on the matter and as a result SFSA could not pursue any further activities. In this ruling SFSA did not take into consideration that minority shareholders at the time had relied on a belief that the Wallenbergs and Investor would ascertain that VW acted in the interest of all Scania shareholders, a position that later was changed.

8.6 Fairness opinion: III.3

A board recommendation of a bid offer may include the opinion of an independent advisor, usually in the form of a *fairness opinion*. In this section this issue is discussed in relation to the Skandia and Capio bids. The EU Takeover Directive does not include any reference to the role of independent advisors. However, independent advisors do play an important role in the UK, were the Takeover Code stipulates that the board must enrol its own independent advisor, different from the advisor that works for the company and its executive management (Rule 3.3). The UK Takeover Code is also explicit about fee payments to the independent advisor:

> Rule 3.3. "...Success fees. Certain fee arrangements between an adviser and an offeree company may create a conflict of interest, which would disqualify the adviser from being regarded as an appropriate person to give independent advice to the offeree company. For example, a fee which becomes payable to an offeree company adviser only in the event of failure of an offer will normally create such a conflict of interest…" (Section D.21).

NBK 2003 lacked reference to any specific obligations related to advisors to the board during a takeover. NBK 2003 stated that independent advice in the form of a fairness opinion was required in case of directors with conflict of interest, and when chosen by the board to be used otherwise, the opinion should be published.[134] However, after the millennium the usage of investment bank advisors during takeovers grew in European countries as well as in Sweden, reflecting an importation of procedures found in the US and UK markets.[135]

In NBK 2009 the text on the use of advisors was amended. Section NBK IV.3 states that it is important that the financial advisor is truly independent of the interest of the bidding party. It states that the fee paid cannot be related to the success of the bid, level of acceptance or if the bid is successful or not. Following NBK 2009 a Swedish board must engage two different advisors to deal with a bid and sales process – one working with the sale and the other working with the fairness opinion. However, the revision 2009 does not go as far as the UK Takeover Code, which demands that different advisors work for the management and the board on an ongoing basis.

The UK Takeover Code (Rule 3.3) also stipulates that it is inappropriate for an advisor that has previously advised a bidding party to act as advisor to the offeree company. The inverse relationship however is not addressed. Neither NBK 2003 nor NBK 2009 mentions the possibility in investment banks of conflicting interests or expectations of loyalty to their customers.

An analysis of both Skandia and Capio reveals a number of conflicts of interests related to enrolled advisors. In the Skandia case, the board engaged the investment bank Morgan Stanley as an advisor, working actively with both the sales process and the preparation of a fairness opinion[136] and then receiving a success fee when the actual deal was finalized. In Skandia the role of the investment bank was unclear also for some of the directors, as the tradition had been that advisors were engaged by the management board and not, as it emerged when the takeover process was unravelling in Skandia, directly on a board mandate.

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[134] Independent advice was required if a bid was made by a concert party with a relationship to board members or during a management buy out.

[135] A personal insider's account of the emergence of US-style investment banking in Sweden is offered in Ramel (2011).

[136] Notably MS opinion was never published.

This conflict of interest was also present during Apax and Nordic Capital's bid on Capio 2006 following, which the investment bank Morgan Stanley both issued a fairness-opinion and worked to entice competing bidders to come forth.[137]

In all three cases – Skandia, Scania and Capio – the question of possible conflicts of interests is highlighted. All cases reveal examples of financial advisors changing sides. In Skandia, advisors prepared bids for multiple parties. In Scania, investment bankers that had worked with Scania on various deals changed employer to Handelsbanken where they instead worked on MAN's hostile bid. In Capio, Deutsche Bank switched from aiding Capio in the rights issue to participating in the bid brought forth by the two PE firms. These dubious actions by advisors would not have been ruled out however if the revised takeover rules had been in place as the NBK 2009 does not address these conflicts.

8.7 Equal treatment of different share classes

Diverging bid premia between different classes of stocks concern the relationship between different groups of shareholders that have stocks with equivalent cash flow rights but different voting power (i.e. Burkart and Lee, 2008). In this section this issue is addressed in relation to VW's activities in Scania and the Icelandic investmentbank Milestones bid on Invik, 2007.[138] The Swedish Companies Act states that all shares within the same class must be offered the same price during a bid, but different classes of shares can be offered different prices. NBK 2003 stated that the difference should be reasonable. However, after the millennium there

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[137] The responsibility of US boards differs from Swedish corporate law, as an US director has a fiduciary obligation to the company during a bid, and is not expected to remain neutral and refrain from taking action.

[138] Jonnergård & Larsson (2009) offer an account of the power play between different actors during the fight to change the price premia for A shares. The account is to a large extent based on articles written by myself in Dagens Industri during in 2007-2008.

seemed to have been a trend towards a reduction of price differentials. As a general guide the Swedish Securities Council indicated at the time that a price differential of ten percent would be in accord with good practise by market actors. [139] At the same time there were a number of large takeovers where the controlling blockholder had not demanded a bid premia. These included Volvo's bid on Scania in 1999, without a premium offered to the block of A shares controlled by the Wallenbergs and Investor in Scania. Similarly Investor and the Wallenbergs did not receive a bid-premia when selling the controlling A shares in Gambro (2006) and VW-Data (2006). MAN offered the same price for the A and B shares in Scania (2006).

This trend was interrupted following the bid by Icelandic investment bank Milestone on Invik, 2007. Then the controlling owner Kinnevik received a ten per cent bid-premium compared to the minority shareholders in possession of B-shares. Through joint activity a group of Swedish and international institutional investors pressed the Swedish self-regulatory committee to bring this to a halt. [140] Institutional investors

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[139] During the period 2000-2005 there were around 25 takeovers of which ten involved a price difference. These varied from 5 per cent to 23 per cent. A more detailed description is offered in a statement from the Swedish Securities Council (AMN 2007:34).

[140] The question of price differential between different classes of shares came to play a role in the MAN bid contest for Scania in 2006, where VW expressed a wish to be paid a premium related to other shareholders. When MAN presented its hostile bid VW CEO Piechtrieder commented in Financial Times that the MAN-bid both needed to be raised and include a bid premium of 10 per cent for the controlling A shares (Nachemson-Ekwall, September 27, 2006, Dagens Industri). Investor and the Wallenbergs did not show any inclination in that direction, and MAN never raised the bid. Thus the general view at the time, 2006, was that the question of bid premium during a corporate-control contest was not an issue any longer (Nachemson-Ekwall, September 28, Dagens Industri). This all changed in April 2007, when Iceland-dominated Racon Holdings, later known as Milestone, bid for Invik. At the time Invik was a Kinnevik controlled firm and thus most of the A shares were in the hands of the traditional owner family Stenbeck. Racon offered less for class B shares than it had recently paid for the class A shares and the voting rights attached to them (SEK 253 and 230 which is equivalent to a 10 per cent premia). Invik's largest institutional

claimed that market practise had changed in favour of equal pricing. According to the institutional investors a bid should be viewed as a liquidation of the company and since all shareholders have the same cash flow rights then the same approach should be used in the opposite situation, that is to say when there is a bid on the whole company. This view can be seen as consistent with the Berle and Means (1932) argument that control is a "corporate asset" and that premiums paid for control go into the corporate treasury (see Ch. 2.5). Manne (1965), however, objected to this, claiming that actors owning control blocks of shares might refuse to sell at a share price which does not pay them a premium at least sufficient to compensate them for the loss of net value present in participating in the governance of the corporation (see Section 2.5).

A group of controlling shareholders (i.e. with A shares) led by private investors closely related to Handelsbanken and Industrivärden sphere, objected. They presented arguments related to either the importance of compensating controlling shareholders for their work with the company (i.e. agency costs) or the necessity of respecting property rights and contractual rights. These two lines of reasoning show similarities with the arguments brought forth in the Swedish defence of A and B shares when the Commission attacked the Swedish model of differentiated voting rights during the work with the 13th Takeover Directive (see Ch. 3.3.3; Burkart & Lee, 2007).

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shareholders, Alecta, AP4, Nordea fonder and Swedbank Robur, believed this was a violation of generally accepted practices. The institutions lobbied the buyers, the sellers, advisers and other stakeholders and expressed their objections, but without success. The Swedish Securities Council deemed the price differential in accordance with good practise. The institutions accepted under protest since they did not want to risk ending up in the minority in an unlisted company. However, they came back, with support from a number of respected international institutional investors. In the autumn of 2007 a letter was sent to NBK and the Stock Exchange OMX, asking for a clarification and amendment of the Swedish takeover regulations so that the same price would apply to class A and B shares in connection with takeover bids, signed by twelve Swedish and twelve foreign financial institutions. These included US-based Calpers, British Hermes, German DWS Investments and the Norwegian NBIM (formerly the Petroleum Fund).

The issue of equal treatment of holders of shares with non-identical terms and conditions was handled in the revision of the NBK 2009. Section II.11 states that, "If the offeree company has different classes of shares, the same form of consideration must be offered for all classes of shares…" One member of the NBK group, Industrivärden CEO Anders Nyrén, made a reservation demanding price differences. NBK also delivered a compromise, where the Swedish Securities Council could grant an exception after special considerations. This applies to a situation when e.g. the owners of B shares are satisfied with the bid but the controlling A-share owner demands a premium and the B-shareholders accept this. Thereby value-increasing bids will not be blocked solely by the demand for equal price. At the time of writing the Council has not yet tested the new rule.

The question of bid premia and different voting rights also play a role in the contexts of the Forced Merger Rule, dealt with in Section 8.8, and the Mandatory Bid Rule, which is dealt with separately in Section 8.9.

8.8 The forced merger rule

The fourth rule group of amendments triggered by activities during the sixth takeover wave in Sweden were dealt with outside the NBK Takeover Rules. These are related to the Forced Merger Rule and the Mandatory Bid Rule. The forced merger (legal: statutory merger) was addressed in the amendements to the Companies Act 2007. The risk that the FMR would be used was relevant in both the Skandia and Capio takeovers and was used by the bidding parties to entice incumbent shareholders to sell, which they also did.

When Sweden after the millennium introduced a Forces Merger Rule, allowing a bidder to acquire all shares once it has gained control of 66 per cent of capital and votes, legal expertise had overseen the capital-market effect of adopting a Forced Merger Rule on publicly traded companies (see also section 7.2.4). By using the FMR a bidder that had gained control of 66 per cent of the shares and votes could delist the company and work to change the corporate charter in favour of activities related to the incorporation of business activities in the interest of the bidding company. This also meant that the bidding party in its initial price offering only had to pay enough to assure that 66 per cent of the shares would tender rather than 90 per cent, which would result in a lower price offer. The problem had an extra twist to it related to Swedish retail funds because these are not allowed to own shares in delisted companies.

In the spring of 2006 both the Shareholders' Association and Securities Council approached the Ministry of Justice with suggestions that the new law be revised. The usage of the FMR was halted in July 2007 through a temporary stop-law that was fully implemented in the Companies Act in 2009.

As stated above, the FMR was a factor in a number of takeovers during the sixth takeover wave, where different shareholder groups fought for bid rises. In Skandia, the risk of being left with unlisted and non-tradable stocks was decisive when a group of institutional investors sold of their Skandia-holdings to Old Mutual in the winter of 2006.

In the Capio case, the Securities Council used a strict legal approach when accepting the FMR, despite the fact that the Securities Council at the time had turned to the Ministry of Justice to review the law and perceived malpractice. For the Securities Council it was enough that the bid vehicle, Opica, had clearly stated in the prospectus that it was to be used (AMN 2006:30, October 2; Nachemson-Ekwall, 29 September, 2006, Dagens Industri). This came as a surprise for market actors as the expectations had been that the Swedish Securities Council, as a self-regulatory body, might have the power to rule against the use of the rule, as it appeared to decrease trust between market participants.

8.9 The mandatory bid rule

A Mandatory Bid Rule, MBR, has played an integral part in forming

European takeover regulation (Ch.6.5). The Swedish MBR has a number of special features that together have worked to increase the ability to pursue arbitrage:

- The rules have been reviewed a number of times.
- The Swedish implementation in LUA differs from the UK Takeover Code, Takeover Directive and NBK 2003.
- The Securities Council has continuously granted exceptions to the rule.

Added together these three factors have made the MBR highly contentious in a Swedish context. Market participants, both investors and companies, have had difficulty both interpreting the exceptions granted by the Securities Council and foreseeing outcomes. The MBR was not addressed in the NBK 2009 revision, but instead remitted to the Ministry of Justice to be handled through a revision of the Swedish version of the Takeover Directive (2006), LUA Act (2006:451).

When the Swedish MBR threshold was lowered from 40 per cent in 2003 to 30 per cent, the aim was to align Swedish regulations to most other European countries at the time and the anticipated 13th Takeover Directive. Shareholders in control of between 30 and 40 per cent of either shares or votes, where not granted an exception to the MBR, thus unable to increase their shareholding without triggering a mandatory bid. However, controlling shareholders with holdings above the 40 per cent threshold were exempted.[141]

However, this changed after 2006 when the MBR was removed from the NBK rules and included in LUA instead. The Swedish Financial Supervisory Authority delegated to the Securities Council the granting of exemptions. The restriction on blockholders with shareholdings

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[141] In 2003 there were only five large Swedish companies with a blockholder controlling between 30 and 40 per cent of the voting-power, and thus affected by the new NBK rules. These were NCC (Ax:Johnson and Nordstjernan), VBG (Herman Kreftings), Ericsson (Wallenbergs/Investor and Handelsbanken/Industrivärden), Skanska (Industrivärden) and Scania (Volkswagen)

between 30 and 40 per cent was abandoned, as it was deemed legally impossible to keep this Swedish exception. LUA was introduced without any public discussion or analysis. However, a closer look at the writing in LUA reveals a number of things:

First, Sweden abstained from introducing thresholds above 30 per-cent (just like Great Britain, Germany and France). However, a number of other countries did. Spain is one example. After a number of reviews, Spain, in 2007 settled for a single control threshold of 30 per cent of the share capital but a dual test of control was retained, applicable in situa-tions where a majority of board-directors were appointed by a significant shareholder with holdings below 30 per cent. Finland settled for a 30 percent trigger as well as a 50 per cent trigger.[142] Denmark and Italy ap-ply a 33 per cent threshold and a 50 per cent threshold. Norway allows companies incorporated in EU-states to comply with their domestic thresholds. For domestic companies and companies outside the EU there is a staggering threshold set at 33 per cent, 40 per cent and 50 per cent.

Second, Sweden grants an unusually high number of exceptions to the MBR. Since 1999 almost two-thirds of the publicly presented rulings by the Swedish Securities Council have related to exceptions to the MBR. Finland for instance seldom grants exceptions. In the UK it is un-common too. The complications with the Swedish MBR emerged from the granting of exceptions that in many cases seemed to be difficult for market actors to foresee.[143] In the following the MBR rule is described as a case of regulatory arbitrage. The take-over fight for Scania is used as illustration with examples from both Sweden and Germany, as VW ap-pears to have been involved in regulatory arbitrage in both countries. In total the prolonged Scania case reveals fifteen breaches of the MBR (*Ta-ble 16)*, in the sense that the intention of regulation was circumvented.

[142] Finland had a previous level of a 2/3 trigger for a mandatory bid.

[143] The complication is mentioned in a statement from the Swedish Securities Coun-cil (AMN 2006:44). It was also an issue when dealing with the question from the Wal-lenberg foundation and Investor related to Volkswagen's share increase in Scania (AMN 2007:08, "Exception to the mandatory bid", public on 7 March, 2007). VW asked for exception when increasing shareholding in Scania up til 49.9 per cent (AMN 2007:36, September 28).

Table 16. The Scania case and the mandatory bid rule 2000–2011

Date	Actions of the misusage of the mandatory bid rule	Involved parties
27/3/2000	VW buys 34 % of votes (18.7)	Seller is Investor
Fall 2003	Investor plans to buy part of Volvos shares in Scania; asks Swedish institutional investors to become co-investors.	Investor, Volvo, Swedish financial institutions
21/6/2004	Investor flags for 15 % in Ainax	Investor, Volvo and Scania
1/8/2004	Wallenberg funds flag for 5.5 % in Ainax	
1/11/2004	W-funds increase ownership in Ainax	W-funds and Investor owns 31.3 % in Ainax
1/12/2004	Investor flags for 21 % in Ainax	
1/7/2006	Adjustment to the Swedish implementation of the EU Takeover Directive	Investor and W owned 29.9 %, still claiming not to act together
7/11/2006	Investor buys 0.3 % of capital and 0.7 % of votes in Scania	Investor surpasses 30 % MBR threshold
24/2/2007	VW increases shareholding from 18.7 % to 20.03%, giving a voting power of 35.31 %	
3/3/2007	VW increases ownership in MAN to 29.9%	
24/3/2007	Porsche passes 30.9 % in VW	Triggers the MBR in VW
17/4/2007	Investor CEO Ekholm thanks for the support given by minority shareholders	
29/9/2007	VW ask if it can buy unlimited amount of shares in Scania	Securities Council consents given there is no change of control in VW.
11/11/2007	Investor CEO Ekholm writes that it is not the strategy to be largest minority investor	
1/12/2007	MAN increases from 14.8 to 15.6 % in Scania	
2/2/2008	Robur and AMF change A shares to B shares	
26/10/2008	Porsche reveals stake in VW	Options to raise stake in VW from 35 % to 75 %, after having added shares from 35 to 42.5 % without flagging
1/1/2009	Porsche passes 50 % in VW	
1/6/2011	VW bid for MAN	Creeping takeover

I use three instances to illustrate: the Ainax case, Investor and VW share increase after the MAN fight, and the relationship between VW and MAN. This section includes material left out from the summarized Scania case in this dissertation (Ch. 7.6) but present in the extended Scania-study (Nachemson-Ekwall, 2012c, Scania, unpublished manuscript).

8.9.1 Ainax

Investor and the Wallenberg Foundation's joint share purchase in Ainax, the holding company which Volvo constructed in the spring of 2004 with the only asset consisting of 24.8% of the votes and 13.7% of shares in Scania, is not addressed in NBK 2009, the Takeover Directive or LUA. The purchase can be described as representing both a breach of trust and a legal violation and as such a precedent that would be central in later circumventions and lack of compliance with the MBR.

On 8 June 2004 Ainax was listed on the New Markets (Nya Marknader), a trading platform owned by the Stockholm Stock Exchange, but open for companies not yet ready for a listing on the Stockholm Stock Exchange, as they did not meet some requirements such as short existing period. At the time, companies listed on the New Market did not need to comply with listing requirements set up by the self-regulatory body NBK.[144] These companies did not comply with the NBK recommendation concerning flagging requirements, set at 5 per cent threshold or the Mandatory Bid Rule.

Shortly after the listing Investor announced that it was in control of 4.2 million shares in Ainax, equivalent to 15 per cent of shares and votes. The reason for Investor's flagging was the upcoming AGM in Ainax, due July 1, at which Investor planned to participate and nominate directors. The activity received much criticism among actors on the stock market. The move was especially startling as Claes Dahlbäck, then chairman of Investor, also chaired the NBK and had been involved in the development of the rules. Investor and the Wallenbergs also continued buying shares in Scania, without flagging. Added together the Wallenberg funds

[144] There were other market places, such as the Nordic Growth Market, an exchange, and Aktietorget, an authorized market place that did comply with the SSE's listing requirements. If Ainax had been listed there, shareholders would have had to flag.

and Investor directly and indirectly through Ainax jointly controlled 25.05 per cent of the votes in Scania.

On 1 November 2004, Scania presented a share bid on Ainax, where shareholders in Ainax were offered shares in Scania in exchange, without bid premium. On 1 December the Wallenberg funds flagged for the control of 21 per cent of the shares in Ainax. This meant that the group directly and indirectly controlled 30.6 per cent of the votes in Scania. This spurred further outrage among market actors. Representatives of the Wallenberg foundation and Investor claimed to be independent parties, approaching the Swedish Securities Council for clearance on the matter. The Wallenberg foundation owned 40 per cent of the voting stock in Investor, and controlled the board through overlapping directorships. The Swedish Securities Council accepted that they be treated as separate legal entities. When a final new set up of Scania shareholders became public in the summer of 2006, the Wallenberg-group owned 16.5 per cent of shares (29.9 per cent of votes). It was still claimed that the two shareholders, i.e. Investor and the Wallenberg foundation, were acting *independently* from each other.[145] Summing up, the Ainax-case includes:

- A circumvention of flagging requirements.
- Two instances of minimalist approach to compliance with the intentions of the Mandatory Bid Rule.
- A questionable interpretation to the concept of related or concert-party.

8.9.2 Investor and VW share increase after the MAN fight

The second case of regulatory arbitrage and the Mandatory Bid Rule emerges from Volkswagens' initial purchase of 18.7 per cent of capital

145 According to SIS Ägarservice, Investor owned 10,7 per cent of shares (19,3 per cent of votes) and the Wallenberg Foundations 5,8 per cent of shares (10,6 per cent of votes).

and 34 per cent of the votes in Scania (1999). The explicit aim was to hold control below 40 per cent, the at the time threshold for the MBR. Investor and the Wallenberg foundation remained shareholders owning close to 13 per cent of the capital and 16 per cent of votes, including both A and B shares. The development later can be seen as an example of skilful agency on VW's part. A number of VW directors used the reoccurring amendments to the Swedish rules to allow VW to work itself into control of Scania, without having to pay a premium to minority shareholders.

To begin with, in the autumn of 2006 VW bought shares in MAN, thus increasing its exposure in Scania without triggering a MBR for the time being (as VW did not yet exercise any formal influence over MAN, but the investment was planned as friendly). The move triggered Investor and the Wallenbergs to jointly increase their shareholding above the 30 percent threshold. The Securities Council looked into the matter but cleared the investment as it did not alter the power balance in relation to the larger shareholder VW, and thus had no implication for minority shareholders (AMN 2006:44).

In the spring of 2007 VW asked for an exception to increase its shareholding in Scania to 49.9 per cent, which it was given.[146] This surprise move gave the impression that there would be a limit at 50 per cent. As Investor stated that it would act in the interest of all Scania shareholders and did not react specifically on the matter, the general public was calmed. From the public information it was not possible for the general public to draw the conclusion that VW could buy an unlimited number of Scania shares if it had asked for a general exception. Since the Wallenbergs also remained shareholders above the 30 per cent threshold the "power-balance" was not altered by the VW move in the spring.

The difficulty (impossibility) for the general public, private investors and institutional investors alike, to understand the implication of the ex-

[146] *Ibid.* (AMN 2007:08; "Exemption to the mandatory bid", public on 7 March 2007).

ception given by Securities Council can be understood when reading the last sentence of the decision made public on 2 February 2007.

> ”Grants Volkswagen AG an exception to the Mandatory Bid Rule which otherwise would have emerged in the case of an additional share purchase in Scania AB. The exception applies to purchases in shares that together represent no more than 49.99 per cent of the votes in Scania.”[147]

However, the real test came in the autumn of 2007 when VW returned to the Securities Council to ask if it could purchase an *unlimited* number of Scania shares without triggering a mandatory bid. VW argued that VW should be exempted from the 30-per cent trigger altogether (since it had owned 34 per cent since 1999). It also requested that, despite a share increase in MAN, VW and MAN should not be treated as concert parties. [148] Again, the Swedish Securities Association granted VW an exemption.[149] A few month later, Investor and Wallenberg sold their remaining shares in Scania to VW, receiving a hefty premium on the trading price at the SSE (also described in Ch. 8.5.3). Minority shareholders reacted with outrage.

Investor CEO Ekholm later said that it is one thing to be largest minority shareholder when the largest shareholder has less than 50 per cent of the control and another thing when the largest shareholder has more than 50 per cent. The legal rights differ.

The Swedish interpretation of the MBR, as it developed by the Shareholders Council, received much criticism from market actors, politicians and media. The critique was focused on the fact that the Wallenbergs had received 200 SEK, left the minority shareholders on their own

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[147] *Ibid*.

[148] 4 October 2006 VW bought 15 per cent of the shares in MAN. On 11 October 2006 MAN announced that it had acquired 14.27 per cent voting interest (11.48 per cent of capital) in Scania. VW increased its shareholding in MAN from 15 per cent until 29.9 per cent on 27 February 2007. At the time VW had 18.7 per cent of the capital and 34 per cent of the votes, and the offer was based on the capital holding alone.

[149] *Ibid.*

and that the Wallenbergs had failed to act on behalf of the minority. As such, the critique reflected the "We-wuz-robbed" position expressed on the London market in the late 1960s (also Section 3.3.2). However, the critique was quickly silenced as the decision was deemed a purely legal matter. But also legal scholars complained, pointing at the unpredictable stance of the Council. Stattin (2006:99) wrote in a comment "One could even ask oneself what is actually the main rule – the Mandatory Bid Rule or the exemption" (quoted in Stattin, 2007:877).

NBK sent a letter to the Swedish Ministry of Justice on October 9, 2009, asking for the introduction of a second mandatory bid threshold at 50 per cent. In the autumn of 2012 no new legislation has surfaced (and it remains unclear why).

8.9.3 Relationship between VW and MAN

The third case of regulatory arbitrage related to the MBR deals with VW and MAN's shareholding in Scania, which grew from the autumn of 2006. When the share increase triggered the MBR this merely resulted in VW offering a bid without premium, so the effect was that VW could just continue to gradually work itself into control of Scania.

In early 2007 the MAN and VW joint investment in Scania surpassed 50 per cent. At the time MAN's offer was still on the table so no one reflected on the matter, as the Wallenbergs had turned down the offer. However, in the spring of 2007 there were speculations in the media that the VW-move also might trigger the MBR from a MAN perspective. LUA 2 Ch.2 §, states that the MBR can be triggered by an indirect change of control. This can happen when a company owns shares in a second company and buys into a third company which owns shares in the same second company and the investment in the second company added together surpasses 30 per cent voting power on the AGM.

However, no one tested the MAN case with the Swedish Securities Council. The issue was politically delicate. At the time Investor CEO Ekholm had clearly stated that the Wallenbergs were acting in the interest of all shareholders, which meant that Scania's minority shareholders felt certain that the Wallenbergs would both remain shareholders or continue working for a higher bid in the interest of all shareholders. Since no party had any interest in another MAN offer, actors remained passive and nothing happened. The Swedish Securities Council could have opened a case itself but chose not to act. However, the Swedish Financial Supervisory Authority (SFSA) opened an investigation, but decided to grant the exception despite having raised questions related to the issue of "Concert party" (see Ch. 8.5.3).

The decision by SFSA is not all clear. Chapter 3, section 4 of LUA, states that SFSA can rule that someone else shall fulfil the obligation to launch a bid if special cause exists. SFSA takes the position that VW should be ordered to perform the mandatory bid, based on the fact that MAN, together with VW owned more than 30 per cent of the votes in Scania. In the ruling, SFSA chose to overlook the exemption that VW had been granted by the Securities Council.

Still, SFSA abstained from taking actions. The reason given was that the exemption given by the Securities Council was legally valid and could only be retried by SFSA through an appeal. Since this had not occurred (an appeal would have had to have been made three weeks following the ruling)[150], the exemption remained valid. This is also the view of Stattin (2007), who goes on however to disagree with the SFSA over the rationale behind the Securities Council ruling, arguing that the main purpose should be to facilitate restructuring (which implies that exemptions should always be the first priority). SFSA instead argues that the principal importance lies with protecting minority shareholders as to maintain trust in the market. The latter view is pursuant to the UK Takeover Code while the former follows the recommendation of the EU Takeover Directive with its twin objective to both enable restructuring of the European corporate sector and guarantee equal treatment of shareholders.

The questions that arise from the actions taken by the Securities Council are why LUA did not include a 50-percent MBR, given the im-

[150] VW bought the Wallenberg's and Investor's shares on 3 March and SFSA presented its view on 10 April 2007.

portance of surpassing the threshold from a legal perspective. As I read SFSA's ruling, SFSA questioned that no party had taken the opportunity to appeal to SFSA. Had they done so, it is possible that SFSA would have ruled that a mandatory bid by MAN, through VW, was required, disregarding the fact that VW had been granted a "technical" exemption.

When Porsche became the controlling shareholder in Volkswagen in 2009, this was finally deemed a change in control in Scania. This triggered the MBR. However, as the bid made then was at market price, offering no premium, investors in Scania were quite cool to the offer and only a few percent of the shares were tendered.

8.10 Amendments to the rules 2012

The Swedish takeover rules were revised an eight time in 2012. Most of these amendments were focused on purely legal and technical issues. Many of the amendments related to the relationship between the board and directors and a controlling shareholder. In the 2012 amendments there is further clarification on the board's obligation to act in the interest of the shareholders (i.e. II.17 and II.19). The board of the target company might for example consider liquidity in the company's stock after a bid has partially succeeded. This might relate to a situation when a controlling party ends up owning 70 per cent of the shares.

One relevant area relates to deal protection. Various forms of deal-protective devices are allowed in Swedish company law but their applicability is severely limited by director's fiduciary obligations to the company. Exclusive party deals might not hinder the board from recommending a better bid or prevent the board from changing its mind if the bid no longer seems to be in the interest of its shareholders. Break-up fees were not addressed in the amendments to the 2009 rules but well in the revision 2012. The case of directors and irrevocable agreements was not addressed by the amendments to of the NBK Takeover Rules 2009 (Stattin, 2010:136). However, irrevocable agreements have been dealt with by the Securities Council in a statement (2008:43) which rules that a director of an un-named company which signs an irrevocable may not participate in the further board work related to the bid. However, no guidance is offered in relation to possible director involvement in the preparatory phase. This targets for example, the role of Skandia director Gardell from the activist fund Cevian, as an investor in Skandia Cevian had signed an irrevocable with Old Mutual while at the same time remaining active on the Skandia board during the bid process. The UK Takeover Code writes extensively on the issue of irrevocable agreements, emphasizing that a director who might have participated in the signing of an irrevocable must make that information publicly known immediately (City Code, section D20–21).

Another area neither addressed in the revision 2009, nor in the amendments 2012, related to flagging requirements. This issue is dealt with instead through the Transparency Directive and supervised directly by the SFSA. However, this means that questions dealing with empty voting, short selling, derivatives and future contracts were not attended to. The question of enticing a bid, putting a company ”in play” and the role of the board can be viewed in the light of different types of deal-protective devices, such as exclusivity arrangements and break-up fees. As stated above these are not addressed in the EU Takeover Directive either but might well be included in the Article 9:2 dealing with preventing frustrate actions. The UK Takeover Code (Rule 21.1) deems any such arrangement unacceptable (without board approval) as they might frustrate shareholder rights to judge the merits of a bid. In British corporate law, as well as US law, there exist fiduciary out clauses. However, The UK Takeover Code does accept inducement fees, if at a low level[151], given that the board deems a bid to be in the clear interest of the shareholders.

[151] UK Takeover Code Article 21.2 mentions a maximum level of one per cent of the bid value.

8.11 Analysis using institutional theory

In this chapter I have described on a case-by-case basis what lay behind the amendments to the NBK Takeover Rules of 2009 and what the (hypothetical) outcome would have been if the rules reviewed had been applicable in the Skandia, Capio and Scania cases. In this section I will analyse in what way the amendments created a more (theoretically) efficient market for corporate control (through facilitating cross-border hostile takeovers). I will lean on Aguilera and Jackson's (2003) actor-centred institutional framework (outlined in Chapters 2 and 3). This will facilitate my work with explaining how takeover-rules, on firm-level corporate governance, work in terms of institutional factors and how these shape how actors' interests are defined. I will also borrow ideas from Aguilera et al. (2007) to structure the interdependencies of these changes in relation to costs, contingencies and complementarities (also outlined in Chapters 2 and 3).

The revision of the takeover rules must be related to the purpose of the original rules and regulations as well as to a contextual understanding of the constituents involved. The goal with the *13th Company Law EU Directive on Takeover Bids* was to create a *level playing field* to increase the efficiency of the market for corporate control in Europe and as a result enhance growth opportunity to be able to compete with the US and Asia. The idea behind the UK Takeover Code was to assure that incumbent shareholders were given fair treatment during corporate-control contests. A third purpose can be traced in the Swedish NBK Takeover Rules as being to assure fair treatment of *incumbent minority shareholders* in a company with a blockholder in control through multiple-voting stocks, mainly by relying on UK regulation but in compliance with the EU to make the Swedish capital market attractive to an internationally active global investor community. These multiple aims have not been all that easy to handle and less easy to develop into a cohesive regulatory framework.

The cross-border hostile bids during the sixth takeover wave in Sweden raised a number of issues. The revised Swedish Takeover Rules

2009 (and 2012) took care of some of these issues. In total 16 amendments were presented in the press release (see Table 15 and Appendix) dealing with the takeover rules in general, mostly resulting in further aligning the Swedish rules with the British Takeover Code.

The amendments belonged to four rule groups. Three groups of were related to the amendments to the takeover rules, as part of the soft law. These addressed actions taken by the bidding party, actions taken by the target board and technical issues. A fourth group of amendments addressed legal regulation in LUA or the Companies Act, i.e. hard law. A number of the new recommendations appear to have been directly related to problems that emerged during the Old Mutual bid on Skandia, Scania and Capio.

Beginning with Aguilera et al.'s *costs* these refer to the value of inputs to corporate governance, such as compliance with existing regulations or opportunity costs of managing relations with institutional investors. In NBK 2009 these costs addressed "technical" issues such as timespan of an offer, announcement-requirements and the role of fee-payment to independent advisors. Also the pricing between A and B shares was treated as a technical issue, as it implied loss of profit for the controlling shareholder who had the power to block an offer if the price was deemed unattractive. Other "costs" include the abandonment of the Forced Merger Rule in the Companies Act and a Mandatory Bid Rule with a 50 per cent threshold[152]. As a result the Swedish takeover rules as of NBK 2009 became technically more aligned to the UK Takeover Code. For the bidding party, and controlling shareholder of the target company this increased the cost for bringing forth the bid. These amendments appear to have been driven by an aim to create a more predictable environment for actors on the market for corporate control, presumable resulting in a more correct — and efficient pricing — of tradable stocks.

Costs in Aguilera et al. can also be related to actions taken by the board of directors, where the board neutrality rule works to enhance the role of directors as fiduciaries of the shareholders. In a corporate-

[152] In the autumn of 2012 Sweden still lacked legislation for a 50 per cent mandatory bid rule.

governance context, such as the Swedish one, where directors are voted in by shareholders for one-year mandate, and can be replaced with short notice by 10 per cent of the votes and capital, this will involve costs related to the directors' ability to make decisions that may have (positive) effects on corporate value creation long-term, but have negative impact short-term (for example on share price). Ahead of a perceived takeover, the risk is that management worries that institutional investors will sell their shares and thus act with a short-term focus on value creation and prevent a bid to being brought forth. Aguilera et al. (2007:14) write: "Opportunity costs may particularly affect the effectiveness of governance in terms of wealth creation".

Aguilera et al.'s organizational interdependency relates to *contingencies*. The Swedish model of corporate governance can be seen to include a number of contingency factors that have formed and influenced Swedish takeover regulation. These contingencies include such factors as strong ownership control, a shareholder-value model of governance and a structure of controlling shareholders through block holdings and multiple voting rights. Historically, the Swedish ownership model was aimed at securing a solid board mandate, in which the board directors could work in accordance with the Companies Act and the directors' fiduciary obligation to act as agents in relation to all shareholders without discrimination with the focus on value creation for shareholders (long term and short term alike).

The most important amendments to the NBK Takeover Rules of 2009 as compared to those of 2003 are those related to the new Rule II.17 and the amendments to Rule II.19. With these amendments there ought to be no doubt that a director must prescribe to the shareholder-value principles of governance, mediated by current shareholders as if that per se is value accretive for society at large. The NBK Article II.19 gives the board a clear signal to take into considerations nothing other than maximizing the economic value of the bid (i.e. the board's view must be consistent with a shareholder-value perspective).

Three other amendments relate to board activities during the preparatory phase of a bid – the target board's dealing with due diligence issues, the role of target directors involved with bidding parties, either as related to a controlling shareholders or being part of the bidding actor in some way, and the role of advisors to the target board in the issuing of a fairness opinion. Some actors that had taken a strong position during the sixth takeover wave, such as investment banks, where pushed back, e.g. in relationship to limits on advisors involvement in the preparation of a fairness opinion. The question of break-up fees, which were not addressed, also belongs to this group of activities.

Another governance issue, related to the preparatory phase of a takeover, enrolment of directors to the board of a Swedish listed company, can be viewed as what Aguilera et al. (2007) call *resource contingency* in the hands of the largest shareholder. Even if a director is supposed to guard the interest of all shareholders alike, since the directors need the support of the largest shareholder/shareholders, they cannot fully be precluded from acting in its/their current interest. The protection of minority shareholders have at the same time been assured by a Swedish tradition, cultural as well as legal, of preventing (monetary) rent extraction from related party transactions (Gilson, 2005). The dilemma of director involvement with a bidding party is partly addressed in the revised NBK Takeover Rules of 2009, which state that a director of a target company related to a bidder or a controlling shareholder supporting a bid shall not participate in the preparation of the target board's activities related to a bid. Three problems appear relevant from the two hostile cases of Skandia and Capio. These are related to time-span, the number of independent directors and the actual definition of independence.

- The lack of a clear cut description of timespan from knowledge to actual deal presentation highlights the role a director might be allowed to play in putting a target company in play in the first place. If a director is deal oriented, i.e. promoting board decisions that might facilitate a takeover, then the director may end up driving the rest of the board towards an inevitable sale situation. (On the Skandia board this deal driven rationale was represented in Chairman Magnusson, Deputy chairman Björnsson and Director Gardell. On the Capio board this deal rational was represented through Chairman Holtback.)

- The Swedish Corporate Governance Code recommends that there are at least two independent directors on the board, i.e. independent from management, customers and owners. It is only a recommendation, which is the first limitation. (Up until 2010 independence was part of the listing requirements at Stockholm OMX Stock Exchange.) Moreover, with only two independent directors, it becomes difficult for the board to evaluate a bid proposal in the interest of all shareholders.

- The procedure for the nomination of directors has not been very efficient in assuring that independent directors are truly independent either. (In Scania, after VW became the dominant blockholder, VW nominated all directors to the Scania board, including those two who were formally independent according to the Swedish Corporate Governance Code.)

Following the Aguilera et al. (2007) framework the third concept, *complementarities*, related to both cost and contingencies, appears to have been at odds with the Swedish model of governance as it came to work in financial capitalism and through the Swedish takeover regulations. One example of this is the BNR, which in a Swedish company with a dominant shareholder, can be claimed to lack relevance.[153] The board is then usually already controlled by the largest shareholder who has enrolled a majority of directors that are positive to the interest of the controlling shareholder. As made clear by Burkart and Lee (2008) this

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[153] The board as a representative (*Sw:* "gestor" or "ställföreträdande uppdragstagare") of the shareholders as a group is discussed in the Swedish Takeover Rules (LUA, Ch. 5, dealing with defence as a passive action). For a general discussion of the passive role of the directors in national company legislation and the Takeover Directive, also see Davies (2010).

facilitates bids because once a bidder gets control of a block of shares, the chances are good that the rest of the shareholders will choose to sell off.

However, in a dispersed shareholder structure the effect of the Board Neutrality Rule is, in a Swedish governance context, different and possibly also distortive, an obstacle to the creation of an "efficient market". A Swedish board of director, in a company without a dominant lacking blockholder, is much more limited in its board-power than its UK counterpart. For example, in a company with an open shareholder structure a new (and to the board of directors, hostile) shareholder can in according to Swedish principles of corporate governance, quickly get a seat on the board, both by acting through the nomination committee or by calling for an extra general meeting.

8.12 Conclusion

Many of the amendments related to the board's behaviour in the takeover regulation 2009 worked to enhance the shareholder-value model of governance. These amendments neither addressed the effect of growing short-termism among the large group of institutional investors nor the presence of regulatory arbitrage conducted by actors in cross-border bids. Rather, the combination of a nomination committee to enrol directors, fully in the hands of present shareholders, does not consider the effect of a possible short-termism agenda governing the interest of shareholders representing index-tracking pension and retail funds, with the effect of increasing short-termism in the boardroom. Nor did the review of the NBK 2009 address possible short-termism among dominant shareholders who might be dependent on support of institutional investors (i.e. a controlling shareholder might own a bit below 30 per cent and feel pressure to act in a way to please the short-term interest of index-tracking institutional investors). In many companies listed on the SSE an ownership of a few per cent may be enough to control the chairmanship, but the usual level is above 10 per cent (which triggers certain minority rights in the Companies Act).

Following the revision of the NBK Takeover Rules of 2009, the short-term – current – stock price appears to dominate the discussion even further. The complementarity between the shareholder focus as stated in rule II.17 and the work of the nomination-committee limited the board's ability to work with long-term value accretive activity. This particular complementarity may thus entail significant cost: short-termism.

In summary, the amendments to the NBK Takeover Rules of 2009 appear to have worked in the direction of enhancing the shareholder-value focus of the Swedish governance model. At the same time this led to pressure to comply with the interests of current – and in financial capitalism often short-term shareholders. The issue of preventing arbitrage (regulatory and moral) was addressed in some parts but not in full, and a number of shortcomings remained. Thus it can be questioned whether the amendments to the Swedish Takeover Rules of 2009 created a (theoretically) more efficient market for corporate control (by facilitating cross-border hostile takeovers).

The eight revision of the Swedish Takeover Rules 2012 did not address the UK takeover panel's concern, as expressed in the tenth revision 2011 (here also section 8.4), with short-termism among institutional investors during a hostile bid. Nor does the revision 2012 address issues related to a board's fiduciary obligation to guard the interest of the corporation during a takeover, as such abstaining from addressing efficiency issues related to other stakeholder groups beside the shareholders.

Chapter 9

Discussion of the results of the studies

9.1 Purpose and structure of this chapter

The purpose of this dissertation has been to study the making (and shaping) of a market for corporate control. I have wished to study its actors, processes and institutions. In particular I have focused on the corporation and its board members, and how the role of directors has been influenced by takeover regulations in the period of financial capitalism. This has created the basis from which I have formulated my research question:

> "How can we understand the idea of a well functioning market for corporate control and the effects of regulatory convergence of different corporate governance regimes (in Europe) in financial capitalism?"

I approach the question through an institutional perspective to bring in notions of social embeddedness and path dependency in corporate governance and include these when approaching the influence mainstream finance theory has had on the regulation of the market for corporate control. A set of propositions are then developed that enable a more dynamic institutional perspective on a market for cross-border hostile takeovers. These were summarized into three hypotheses (section 3.6):

> *Hypothesis 1:* A corporate governance model contingent on ownership governance has difficulties in its quest to balance the value accretive strategy of directors and executive management with financial capitalism's one-sided preference for (current) shareholder value and liquidity over more stakeholder oriented governance models.

> *Hypothesis 2:* Institutional investors investing according to portfolio theory and with a preference for shareholder value governance may push corporate directors and management towards short-term strategies and facilitate cross-border hostile sell-outs.

> *Hypothesis 3:* Open and liquid capital markets with globally active investors investing in domestic capital markets with diverging corporate governance systems enable arbitrage, both regulatory and morally.

The next step has been to frame the empirical parts of the dissertation in the Swedish institutional setting of the sixth takeover wave. This includes a description of the Swedish shareholder friendly corporate governance model and its particularly active market for corporate control. This led to a reformulation of the three hypotheses to make them applicable to the specific Swedish setting (also Ch. 6.8). To explore their validity, three longitudinal case studies of cross-border hostile takeover processes involving Swedish targets have been conducted. I have explored in what ways these processes can be related to the ideas behind the creation of an efficient market for corporate control. Lastly, I have studied different takeover regulations to find out in what ways a shareholder oriented revision of the Swedish takeover regulation in 2009 addressed problems related to the (theoretical) creation of an efficient market for corporate control.

This analysis answers calls from Aguilera and Jackson (2003) to integrate dynamic factors from financial capitalism. In this dissertation sociological, organizational and dynamic factors are integrated to better explain the outcome of a cross-border corporate control contest. Finally, to interpret my findings, the institutional framework developed by

Aguilera et al. (2007) is borrowed and an "open systems" approach to understanding organizational interdependencies is used. The analysis of the building blocks is developed in the next section (9.2). Each of the four empirical case studies are then analysed separately (Section 9.2.1) before explaining the amendments included in the 2009 revision of the Swedish Takeover Rules in terms of the concepts of path dependency, social embeddedness and regulatory capture of corporate elites (Section 9.2.2). In the *Conclusion,* I deliver my answer as revised hypothesis (Section 9.3).

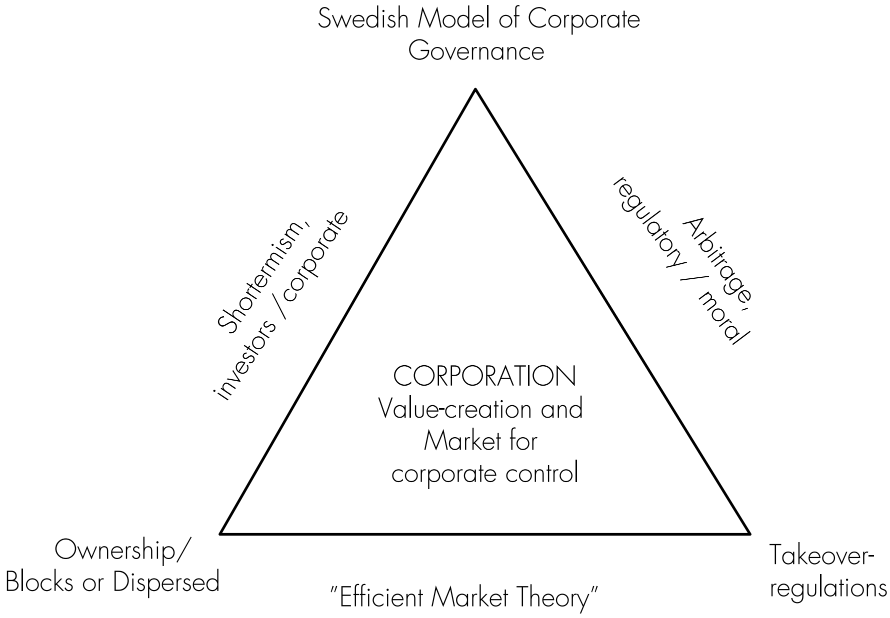
9.2 Analysis

9.2.1 Open systems approach

A central theme of this dissertation is the institutionally oriented theorists' view, as professed by Fligstein and Chou (2005), claiming it is complicated to import governance models from one country to another. Importing some institutional features linked to economic growth in one country will not automatically cure inefficiencies or generate high growth in another. Rather, the importation of another country's corporate governance conventions are not likely to work unless the entire system is borrowed or the borrowed mechanism (s) fit (s) with what already exists in a given society. Grounded on this reasoning and as described in section 3.5, I turn to Aguilera and Jackson (2003) and their actor-centred approach to understanding diverging models of corporate governance. This model stresses the interplay of institutions and firm-level actors and argues for a further integration of interdependencies in the convergence debate (Aguilera & Jackson, 2003, p. 448). I also follow calls from Aguilera et al. (2007) to analyse how these interdependencies between the organization and diverse environments lead to variations in the effectiveness of different governance practises. In this dissertation, the target governance practices are those relevant to takeovers, in particular takeover regulation and the actions of directors during a hostile takeover in general, and a cross-border hostile takeover process specifically. The inclusion of interdependencies is especially important when trying to understand the effects of importing different rules and regulations, and why convergence does not necessarily generate the expected outcome (Jackson & Miyajima, 2007). At the same time, it is equally important to develop an analytical model that can cope with what emerges when an imported change has not generated the expected outcome. With this in mind, I suggest a revision of the Aguilera and Jackson (2003) model that include additional dynamic factors, where actors' behaviour (as reflected by the national model of corporate governance) in financial capitalism is integrated. *Figure 13* ("Dimensions of corporate governance in financial capitalism") summarizes some of this dissertation's empirical findings and anticipates the hypothesis that emerges from those findings, all of which hinge upon short-termism and regulatory arbitrage. Mainstream finance's "efficient market theory", with its rational human being theory, is included as a factor that helps explain financial capitalism. The illustration should be viewed as both multi-dimensional and multi-factorial where related concepts form a web of interdependencies in both time and space. With this hypothetical model in mind, I turn to the case studies, with special emphasize on the last study of the amendments to the Takeover Rules of 2009.

In the *Old Mutual-Skandia case*, the dynamics of corporate governance, the market for corporate control and takeover regulation all involved a new set of actors, not related to the historical governance context, lacking both path dependency and social embeddedness (Granovetter, 1985) These new actors included the shareholders involved, foreign and domestic institutional investors and hedge funds as well as activists that as a group were governed by a strictly rational activity mediated through quantitative restrictions, portfolio theory, index tracking and current "short-term" shareholder value logic. The Skandia case also involved a new set of middlemen, such as Anglo-American influenced investment banks and globally active legal advisors.

Figure 14. Dimensions of corporate governance in financial capitalism



Ibid. After figures 1 and 3

Thirdly, a legal framework imported from both the UK and the EU, encompassing both soft and hard law, did not generate the expected outcome, i.e. a level playing field among corporate actors; instead it emerged as enabler of regulatory arbitrage. The rationally bounded human beings (Simons, 1957) also participated in this transformation, as shown for example by how directors on the Skandia board came to interpret their fiduciary duty differently, depending on where they situated their rationalities along the operative or financial flow in the governance of the corporation (Östman, 1993, 2008; Sjöstrand, 1993, 2005).

The *Apax/Nordic Capital-Capio case*, given its many similarities with the Skandia case, can at best be described as a "hyper Skandia". Just like Skandia, Capio had a dispersed set of owners, of which many were institutional investors regulated by limiting quantitative rules, with an index tracking portfolio strategy and ready to sell for short-term profit. Just like

Skandia, the investment bankers designed the bid to leverage on regulatory and moral arbitrage. Examples of these arbitrage opportunities were threatening to use the Forced Merger Rule, circumventing due diligence procedures and *stretching* the meaning of a "friendly" bid. Also, as in the Skandia case, Capio appeared to have competing rationalities present on the board of directors.

The *MAN-VW-Scania case* mainly provides regulatory arbitrage by actors emanating from different corporate governance regimes. The bid fight is full of examples of incumbents challenging the takeover rules in different ways, be they Swedish rules, German rules or rules emanating from the EU Directive. All in all, the whole Scania story, with its fourteen years time span, included fifteen breaches of the Mandatory Bid Rule. These breaches by the controlling shareholders can be explained through the bargaining power of incumbent elites and their ability to influence the outcome of soft and hard regulation and as such occupying the space available for decision-making in democratic countries (Hancher & Moran, 1989). Scania can also illustrate the effects of the clash between the general quest for a "level playing field" among corporate actors (in Europe) and different degrees of shareholder orientation to both national corporate governance and takeover regulations. The cross-border hostile takeover of Scania becomes an example of perversion of a regulatory environment were constituents protected by controlling domestic devices are free to act across borders with the effect that a less protected target will not only be acquired, but the outcome will be an overall reduction of the number of actors able to compete on the market for corporate control. This will work against the emergence of an efficient market for corporate control and reduce its role as catalyst for long-term welfare creation for society at large (Jackson & Miyajima, 2007; Davies et al., 2010).

It seems fair to say that at the start of the sixth takeover wave the Anglo-American shareholder value model of governance was well integrated in the Swedish governance environment and the takeover regulations, as it fit well into the historical context of the Swedish Companies Act and a controlling shareholder regime. However, the Swedish governance environment looked quite different to those in the US and in the

UK. The US has a different corporate law, different view of corporate control and a different approach to the legal role of the board and management during a hostile takeover. An American board can fend off a bid with the argument that it is not in the interest of the company's long-term business proposition. The Swedish environment also differed from the UK, from where Sweden imported both codes of governance and takeover regulations. The differences were very apparent in relation to actions taken by institutional investors such as pensions funds, hedge funds and retail funds. Swedish institutional investors have been able to be very active as corporate governors. In the UK institutional investors have been more or less "passive" investors. In the US institutional investors' position has been limited from the start, reflecting (current) shareholders' weak position as corporate governors.

Thus, in Sweden, with its particularly shareholder friendly governance model, a high presence of institutional investors, domestic as well as foreign, made Swedish firms very exposed to the pressure of external institutional forces, such as globally active pension, retail and hedge funds. When the Swedish market for corporate control developed during financial capitalism, through the importation of regulations and behaviour from the US and UK (and EU), the market for corporate control in Sweden ended up working differently than in these two countries. In Sweden short-termism and regulatory arbitrage emerged as important forces and decisive factors during a corporate control contest in the sixth takeover wave.

Many of the amendments to the NBK Takeover Rules of 2009 appear not to have been aimed at dealing with these problems. In the Aguilera et al. (2007) framework these problems can be seen as costs related to the creation of an efficient market for corporate control. From a theoretical perspective, the greater part of the amendments of 2009 did not address issues to assure that the hostile takeover mechanism works to assure that "better companies", defined as "better management", can take over less well performing companies and fires "bad management" (Manne, 1965) and as such assures that management feel the pressure to work to enhance value creation in the interest of shareholders (Jensen &

Ruback, 1983). Rather, the revision 2009 (and the follow up 2012) seems to have been focused on three other issues:

- Maximizing price and enhancing the board's involvement in the completion of the sales process. In effect, this has increased the tendency towards short-termism among actors.
- Levelling the playing field between the shareholders of the target company and the bidding party to create a more efficient price, defined as a price reflected by available information equal to all actors. This work has focused on technical issues within takeover rules rather than regulatory arbitrage between different regulatory systems.
- Levelling the agency cost between controlling shareholders and minority shareholders in relation to the bargaining power over price. However the revision did little to limit the controlling shareholder's work, through its directors, during the pre-bid phase.

Added together, the amendments to the Swedish Takeover Rules 2009 did not address problems experienced by a target company with a dispersed shareholder structure and high presence of institutional investors. Rather, the changes worked to enhance the bargaining power of the owners, as a collective, in relation to the board of directors. This can also be described as more control given to shareholders, less to directors, and as such further limiting the directors' scope of action in relation to both its fiduciary responsibility in the Companies Act (working for the shareholders as a group with different investment horizons) and the Capital Market law (i.e. working for previous, present and future shareholders).

From the perspective of the board I argue that some of the amendments to the NBK Takeover Rules of 2009 decreased the board's ability to act for the company long-term in such a way that this represents a breach against both the theory of the firm and company law. In the Aguilera et al. framework the result of a governance mechanism is contingent on the interaction with the regulatory and institutional environment. In a setting that enhances a governance model based on a shareholder focus, and this model interacts with an institutional environment with a high presence of short-termist investors and ability to pursue regulatory arbitrage the board's ability to work for the value accretive prospects of the target company is reduced.

The revision of the NBK Takeover rules of 2009 (and the amendments of 2012), claiming to produce a supposedly (more) efficient market built on a shareholder contractual principal-agent relation, did not take into consideration the institutional environment with growing short-termism among shareholders and regulatory arbitrage by actors from differing governance regimes. Rather, the revision of the takeover regulation strengthened the governance flow emanating from the financial rationality in the Östman-Sjöstrand model of forces governing the value-building process of the corporation (described in section 2.3.1).

9.2.2 Social embeddedness and (corporate) elites

To see how the lack of compatibility between the revision of the Swedish NBK Takeover Rules of 2009 and the rest of European takeover regulation best be understood, it is necessary to move the analysis to the why-question. Why did the Swedish takeover regulation when revised in 2009 (and again in 2012) move further along the shareholder value path? As a result of this shareholder focus the Swedish takeover rules diverged from the rest of Europe, at least in relation to the board's role as pointed out in both the EU Takeover Directive and the UK Takeover Code.

To analyse this I introduce a dynamic perspective in the Aguilera et al.-model related to how different actors have positioned themselves during a takeover process, changed the power play and influenced the development of the level playing field. In terms of the analytical framework of interdependencies developed by Hancher and Moran (1989), Swedish self-regulation has, within the democratic structure of Swedish parliamentarism, opened up for regulatory capture (from lobbyist groups) and bargaining (between parties of various strength).

Aguilera et al. (2007) claim that it is crucial to supplement the concept of path dependence with the concept of complementarity in order to understand the dynamic properties of corporate governance systems. Additionally they argue that if complementarity is recognized as a cause of path dependence, one can derive that increasing convergence pressure may even lead to a convergence towards an inefficient system. This is also a conclusion drawn by Schmidt and Spindler (2002):

> ”For the case of corporate governance systems shaped by complementarity, that there is even the possibility, of a convergence towards a common system which is economically inferior. And in the specific case of European integration, "inefficient convergence" of corporate governance systems is a possible future course of events.” (Schmidt & Spindler, 2002:3)

I would say that in the case of the amendments to the Swedish Takeover Rules of 2009, with its strengthening of the power of short-term actors, there are indications from the studies in this dissertation that this might possibly have been the case. I would argue that it is possible to hypothesize that the actors that have dominated the regulatory space of the Swedish takeover rules (through self-regulation) are made up of a combination of the (short-term) institutional investors, traditional controlling shareholders, and legal expertise and investment bankers paid by the two previous groups. The corporation – the employees and the CEO of the corporation alike – have not been represented in the discussion at all. Representatives of the Stockholm OMX Stock Exchange and the stock market in general have been left out too.

In Sweden the shareholders, the incumbents and institutional investors alike, had a common interest in strengthening the power of the shareholders, albeit for different reasons. The influence of these groups might possibly be explained by the fact that a prerequisite of the Swedish ownership model of governance, with its strict shareholder value focus, was the presence of long-term responsible investor-owners, often described as the old capitalist of “flesh and blood” (in contrast to “faceless” anonymous institutional investors) as well as a captive and regulated domestic capital market. In financial capitalism the Swedish capital market work differently: the controlling owners have decreased both in size and number and are more prone to act according to expectations of global active institutional investors.

In Sweden the push towards regulatory convergence was intensified by institutional investors' increased role in the enrolment of directors to the board. But Swedish nomination committees do not seem to work as expected either. Controlling shareholders do not always actively involve institutional investors in the nomination process of directors. At the same time the governance of companies with a dispersed shareholder base remains in the hands of short-term institutional investors. This does not mean that the institutional investors' participation in the nomination committees does not work, but they can only be presumed to do a good job long-term in well performing companies with a stable shareholder base. Jonnergård and Larsson (2009) explore the limits of the work of institutional investors. Despite successful pressure from institutional investors to eliminate differential price for A and B shares during a bid, an exception to the rule was included in the final revision of the Swedish Takeover regulation 2009 (Section 8.7).

9.3 Conclusion

In this dissertation I have taken a closer look at the development of takeover rules in a national European setting. I conducted six studies. The first two were background descriptions of the institutional setting of the Swedish governance environment and takeover market. I then used three longitudinal case studies and made one in-depth analysis to describe how the takeover rules, and revisions of them, addressed problems related to the creation of an (theoretically) efficient market for corporate control (by facilitating cross-border hostile takeovers). The findings are incongruent with modern finance research and the ideas behind the quest for regulatory convergence as a means of creating an efficient market for corporate control. The expectation has been that converging regimes of corporate governance will result in a dispersed shareholder regime, where liquid capital markets (with lower cost of capital), a strict shareholder value model of governance and a vibrant market for corporate control open the door for hostile takeovers across European national borders (Rajan & Zingales, 1998; Becht, 2002). However, the finding appears to be more consistent with the *Varieties of capitalism literature*, showing that models of corporate governance are both embedded in different local contexts and path dependent (Coffee, 1991, 1999; Bebchuk & Roe, 1998; Hall & Soskice, 2001). But this is not enough. The case studies and the description of the development of the regulatory framework also exemplify a lack of convergence towards a dispersed shareholdership (Kallifatides, Nachemson-Ekwall & Sjöstrand, 2010; Henrekson & Jakobsson, 2012). There is a growing tendency to question whether convergence is actually taking place (Pacces, 2010). I would argue that the question rather becomes what emerged instead when regulations are changed and appear to have achieved a different than expected outcome. Understanding this outcome has been the principal finding of this dissertation.

9.3.1 Hypothesis

I have chosen to present my conclusion as a formulation of three final hypotheses and a few sub-hypotheses that encompasses both the hypotheses presented in the conclusions in chapter 3.6 and the transformed Swedish hypotheses in chapter 6.8 developed in this dissertation: The *first final hypothesis* deals with national governance regimes in financial capitalism.

> *Final Hypothesis 1:* The particularities of a national governance regime play a role in the outcome of a contest for corporate control.

> *Sub-hypothesis 1b:* A governance regime with strong shareholder governance will be more open to cross-border hostile takeovers than regimes with more of a stakeholder orientation.

In the Swedish context the outcome of a cross-border hostile takeover has been influenced by different soft and hard regulations. During a corporate control contest the board has to submit to three different interpretations of the director's duty:

- To represent the company's interest as expressed in the EU Takeover Directive and in the Swedish LUA.
- To represent the company's interest as expressed through the shareholders in the self-regulatory NBK Takeover-rules.
- To represent the company's interest as expressed in Swedish corporate law.

Stattin (2009) reasons that in a legal area with an over-reaching aim to provide a financially sound outcome, but with three seemingly competing interpretations, the most efficient interpretation should be the interpretation judged most efficient by the Swedish takeover rules. The one that has governed development of Swedish takeover rules is the Fama (1983) definition of efficiency as the price that is reflected in the stock price. This stock price can be seen as (over time) reflecting the best approximation of the market value and as a result also act as an indicative of value creation "for society at large". What is clear is that takeover regulation has increased the directors' ability to work for "present" shareholders, as well as its ability to work for a higher bid ("in the interest of all current shareholders"). Given the institutionalist perspective here it is not clearer that the focus on the shareholders and deal activity have made the takeover market any more efficient from a societal perspective.

The *second final hypothesis* deals with the role of the board. The focus on a board's passive role during a bid stops short of addressing a situation where a company is put in play, but there are no competing bids (such as the case of Skandia). From this follows that in an environment with a high number of institutional investors governed by a short-term index-tracking rationality this may have a major impact on the outcome of a hostile bid.

Final Hypothesis 2: The rationalities of institutional investors play a role in the outcome of a contest for corporate control.

> *Sub-hypothesis 2b:* Short-termism (as compared to long-term corporate value creation) among institutional investors will increase the chances of the success of a cross-border hostile takeover.

The *third final hypothesis* targets the presence of bounded rational human beings and their importance in the cross-border hostile takeover process.

> *Final hypothesis 3:* Different degrees of skilful agency affect actors' ability to influence the outcome of takeover process.

> *Sub-hypothesis 3b:* Those actors that are placed in a central position in the regulatory network have greater chance of influencing the development of the regulatory framework in a direction that is consistent with their own interests going forward.

In financial capitalism those central actors can be described as lawyers and investment bankers ready to interpret the takeover rules in the interests of deal driven institutional investors and owners. Thus the investment bankers and lawyers *have replaced* the corporate directors and executives as agenda setter for the value accretive process of the corporation.

So what does this imply? In Sweden institutional investors (with the support of an array of middlemen) appear to have taken over the market for corporate control. In the Swedish governance context the nomination committee has become the catalyst for corporate control working in two opposing ways. On one side, in companies were there are no controlling shareholders, short-term shareholders have taken control. In companies that still have a controlling shareholder on the other hand, this investor has strengthened its control. The institutional investors have surrendered in the sense that they accept a subordinate role in companies with controlling shareholders, without the influence originally intended with the introduction of nomination committees. One outcome of this is that independent Swedish directors are only sometimes independent.

9.3.2 Theoretical contribution

This dissertation contributes to related literature on comparative corporate governance. I will highlight three contributions related to an institutionalist organisational perspective.

First, this dissertation calls into question the fundamental conditions underlying the concept of a market for corporate control. According to Manne (1965), these are, as presented in section 2.5:

- There is a high positive correlation between corporate managerial efficiency and the market price of shares of that company. This will hold true over a period of time, as the market price will more or less reflect true value, and there are no other real measures of managerial efficiency.

- There is dispersed set of shareholders, viewed as pure (profit-maximizing) rational financial investors in a Berle and Means sense, with the right to sell to another buyer when dissatisfied rather than relying on either the business judgement or the fiduciary duties of directors and management.

- Adolf A Berle's contention that control is a corporate asset must be wrong. The implication of Berle's notion is that any premium received by an individual for a sale of control belongs in equity to all of the shareholders.

The Swedish market for corporate control during the sixth takeover wave did not resemble an efficient market in the sense that the stock price reflected the long-term value of the corporation, and the shareholders traded in the stock according to long-term expectations. Instead the outcome, and the pricing, resembled short-term relative price expectations and an index-tracking rationality of institutional investors.

The problem with this is that in a situation where the share price diverges from a perceived reasonable long-term value, a party with exclusive or supreme knowledge could take the role as guardian of the corporation. In Swedish company law, the role of the guardian has principally been granted to the board as the shareholders' agent in a collective sense (Sw. "gestor"). However, given the board's neutral and passive role during a hostile takeover of a Swedish listed company this balancing mechanism is not always functioning. This is especially clear during a cross-border bid fight.

The dissertation also calls into question the particular quest for a corporate governance regime built on Berle and Mean's dispersed shareholdership. Hansmann and Kraakman (2001) point out that globalization seems to have resulted in a convergence of national company law and governance. Hansmann and Kraakman point to the emergence of a public shareholder class as a broad and powerful interest group in both corporate and political affairs across jurisdictions. Implicit in this reasoning is a drive to minimize agency cost, described as the principal-agent relationship (Jensen, 1976). However, the Swedish model for corporate governance facilitated hostile bids, not because the Swedish governance model facilitated value accretive takeovers on a market with rational actors active on an efficient capital market, but because the model enables short-termism and regulatory arbitrage (between different and thus imperfect national markets with some actors maximizing profit based on their different and sometimes contradictory rationalities).

In addition the third Manne contention that the value of the company ought to be viewed as a tradable asset to be distributed between shareholder groups related to their bargaining power can be called into question, i.e. the Manne vs. Berle-Means debate. The question is not which view is to be seen as correct, but it is necessary to develop a consistent application of one standpoint or the other. In a governance regime with a strong shareholder influence and a blockholder culture, a mandatory bid rule might be easy to circumvent by the incumbent investors and their rivals. This will produce an outcome that is less beneficial to minority shareholders, the very group of investors that the mandatory bid rule aims to protect in the first place. In the opposite way, a governance regime lacking a mandatory bid rule both requires an openness to differential prices and means for minority shareholders to challenge decisions by the board and the (new) large shareholder in court. This raises the question of whether it is ever possible to take a position on the advisability of a mandatory bid rule without seeing the market for corporate control in a national context embedded in a historical institutional setting?

The dissertation's second contribution to the literature relates to Aguilera and Jackson's actor-centred institutional approach to corporate governance. Here this is applied to a cross-border hostile takeover-process. A one-sided regulatory focus on equating "market efficiency" with the concept of shareholder value has led to price as the only decisive factor during a hostile bid process. When a dynamic perspective is applied, showing how a revision of the takeover rules further weaken the directors' role as guardians of the corporation during a hostile bid, the directors have in fact been thrown into the jaws of current, often index tracking and short-term institutional investors.

This dissertation also makes a third contribution, which I would say is adding to the literature of rational decision-making. If the market for corporate control cannot be claimed to be efficient in general, and the cross-border hostile market is specifically ineffective, it becomes difficult to claim that the actors participating in the takeover process behave like utility maximizing rational actors. Rather, the actors make decisions both grounded in bounded rationality (Simons, 1957; Aghion & Tirole, 1997), the position they play in society (Crouch, 1986, referred in Hancher & Moran, 1989; Scott 2001) and as multi-rational human beings, i.e. also influenced by feelings and culture (Sjöstrand, 1997).

The effect is that in an environment with financial capitalism, a high presence of index-tracking institutional investors and a high dependency on a shareholder-value model of governance and regulation, the bargaining power of the corporation is weakened and the directors are unable to enhance the operational dimension of the company's value creation long term. Relating to Sjöstrand (1993, 2005), Östman (1993, 2008) and Kallifatides, Nachemson-Ekwall & Sjöstrand (2010) and their description of the two flows governing the value building process of the corporation, the dissertation gives ample evidence of financial capitalism governance being tilted in favour of the financial flow. This has been enhanced by a regulatory push in favour of deal making (short-term). Therefore, the role of institutional investors might have to be reviewed in favour of long-term value creation. This reasoning is congruent with the work of Hawley et al. (2011) that claims:

> ”Years of focus on the fiduciary duty of prudence has generated myopic investment herding behaviour, undermined inter-generational pension equity, and disrupted attention to the fiduciary duties of loyalty and impartiality. Reclaiming fiduciary duty balance between prudence, loyalty and impartiality is critical to sustaining pensions promises”. (Hawley et al., 2011:1).

Thus, by aligning the investment horizon of employees and future pensioners the value creation process of listed companies will be enhanced.

9.4 Concluding remarks

9.4.1 Generalisation

A study of the Swedish takeover market during the sixth takeover wave, its process, actors and institutions, can be used as a case in the growing field of literature on converging corporate governance. The Swedish experience – its shareholder friendly governance model, active market for corporate control, takeover rules, amendments to regulations and how these factors all work together in a national setting – can give insight into how a national market for corporate control might work when exposed to global financial capitalism. There is a growing body of literature questioning whether convergence is taking place, and in that context the three case studies of cross-border hostile takeovers provide ample illustration of possible pitfalls in the process. This dissertation especially contributes to a questioning of the whole idea of cross-border hostile takeovers and an efficient market for corporate control. This question touches upon governance systems and takeover regulation in many other countries, both in Europe and elsewhere.

9.4.2 Suggestions for further research

This dissertation generates a series of future research topics. Becht (2002) wrote that the EU Takeover Directive, with its focus on the level playing field and resulting quest for reciprocity in implementing new regulations, would not do much more than increase regulatory complexity and confusion in the current systems of corporate control in Europe. Berglöf and Burkart (2003) warned of introducing pan-European regulations without prior economic analysis, arguing for the importance of understanding what new rules imply for existing ownership and control arrangements in Europe. This dissertation supports these concerns and highlights the need for more qualitative studies in the field of cross-border hostile takeovers.

Understanding how Swedish takeover regulation actually works requires an understanding of how takeover regulation works in other countries. Most international research has focused on comparative corporate governance related to board structure and corporate law. Most studies have been quantitative. There have not been many qualitative studies dealing with how changing regulation has influenced corporate actors. Thus there are few studies that highlight the questions of short-termism and regulatory arbitrage as issues for policymakers at both a national and international level. It would be valuable to see studies similar to this one but with data from other European countries. British regulation has for example been revised a number of times, the most recent 2011 (the tenth revision). The European Commission plans for a revision of the Directive 2012.

A third area for further research might be to address possible policy changes to level the playing field by involving more stakeholders and actors in the cross-border hostile bid process. It could be studied how possible short-termism among institutional investors can be dealt with through policy changes, the implication of possible limits to index-tracking behaviour and the effects of aligning the goals of portfolio-managers more with the long-term interest of the fiduciaries, e.g. future pensioners. This might include changing incentive systems. It could also be relevant to take a closer look at the role of sovereign states in the guarding of "national champions", done with a sustainable value building perspective free from ideology.

It could also be valuable to study what the result might be if long-term investment strategies are encouraged among institutional investors while at the same time participation in the governance of the firms is enhanced. Along these lines follows a discussion of the possible effects of a revision of capital markets regulation to make the board's role more clearly reflect the fiduciary obligation to the company rather than drift into passivity during a hostile bid-process. From this follows further rethinking concerning the preparatory phase of a bid, due diligence activities and the possible conflicting roles of directors also related to large shareholder groups.

From a Swedish perspective, the work of the Swedish boards can be researched further. This includes developing theory to handle director independence and integrity both in relation to shareholders as a group and to specific blockholders as stakeholders. What would it mean for the value accretive process if board terms were extended to two or three years, with overlapping terms, or if independent directors' position was strengthened? At the same time the way the nomination committees work might be changed to promote a more long-term focus of its members. This could possibly imply that only investors, with a stated long-term interest, would participate, neutral representatives be included and possible more directors from the board (e.g. two or three).

9.4.3 Personal endnote

I started initial work with this dissertation at the top of the financial bubble in December 2006 with just a simple question in mind. Why was it that Skandia was bought up by Old Mutual? Six years later I must admit the answer was more fascinating than I ever could have imagined. As a personal reflection I would say that the results related to cross-border hostile bids during the sixth takeover wave reflect an active takeover market, but it is doubtful that it reflects an efficient market for corporate control. Rather, it leaves me with a more multidimensional question: What if a shareholder friendly model for corporate governance, accompanied by shareholder friendly takeover rules, does not lead to the creation of an efficient market for corporate control, but rather results in rent-seeking from certain groups of actors participating in the takeover process itself – that is middlemen such as lawyers, investment banks, corporate managers, directors and (short-term) institutional investors (i.e. are richly paid for involvement without actually contributing to the value creative process)? This leads to an even more elusive question: what can be done if there really doesn't exist an efficient market for corporate control at all. In this dissertation I abstain from delivering an answer. Instead I refer to Manne (1965) and his ideas on the best way to create a more efficient market for corporate control, which were negotiated mergers between friendly parties, rather than tender offers, proxy-fights or takeover-bids.

> "Mergers seem in many instances to be the most efficient of the three devices for corporate takeovers. Consequently, they are of considerable importance for the protection of individual non-controlling shareholders and are desirable from a general welfare-economics point of view."(Manne, 1965, p.11)

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Appendix

1 The Skandia case study

The Skandia narrative also belongs to postmodern literature through which the Skandia narrative moves away from the central question of traditional hermeneutics "what (the takeover) happened?" to the post structural analysis of "how did it (the takeover) happen?" (Czarniawska, 2001:101). The question that was addressed in studying Old Mutual's hostile takeover of Skandia 2005 was then a simple one: How and why did it come about?

The empirical work was carried out from December 2006 to March 2008, with follow-ups well into November 2008. With my background I could quickly construct a list of those people we wished to approach. The list included some hundred names. We were not able to meet all of them, notably as a consequence of the lack of openness in British corporations compared to the Swedish corporate tradition. We did meet a dozen of people in London, but chose not to visit South Africa. The British control also had effect on Skandia, which became less accessible after the takeover than previously.

The grounds for the descriptions were in the end part interviews with 75 people, some lasting up to four hours, some repeated two or three times, with people with insight in the processes covered. The description also rests on documents published by the targeted companies, almost everything reported in the Swedish media, a selection of the reporting in the UK, the US and the South African media, and more than 50 analysts' notes.

All interviews were open-ended (Noaks & Wincup, 2004:80). This method was chosen as to maximize flexibility, enabling active listening and enhance trust between interviewee and the interviewer. It is also very useful as research method for accessing individuals' attitudes and values (Byrne, 2004:182). A typical setting could be as follows:

- We sent an introductory letter, asking to schedule interviews and explaining the purpose of the study, which was to answer the question Why Skandia was taken over.
- Most of the meetings, if not all, had to be followed up by telephone to "persuade" people to tell their story, as most of them were bound by confidentiality agreements with their employer, either Old Mutual or Skandia.
- A first meeting would begin with us asking the open question "Describe how the takeover came about from your perspective?" Our role was initially to help actors with their memory – giving enough hints to enable the interviewees to remember events.
- During the interviews notes were taken by hand, by both of the interviewers. None of the interviewees wished to be recorded, thus enforcing the confidentiality and "off-record" setting. Given this restriction, it was good to be two people doing the questioning and note taking.
- The interviews were transcribed in as much detail as possible within one or two days, which was necessary to preserve memory.

With the interviews in hand we looked for new information, patterns and values. These bits and pieces were followed up methodically. For example, if a board member referred to something in an analyst report we would make sure to obtain a copy of the same report, and if possible interview that analyst too. Having read the report we might then return to the board member for further questions and clarification or turn to other board members to check the value of the information. In the second round of interviews we could pose more critical questions; referring to new facts, pointing out inconsistencies and challenging "dubious" explanations on their part.

Thus the research process, based on interviews, resembled a detective's working procedure when looking for clues in order to reconstruct the past. Crucial to this process was to continuously keep an open attitude towards the material, always ready do reconsider an assumption if new facts were revealed. The interview process thus came to rely on the common sense logic of grounded theory, always going back and forth between the empirical material and theoretical knowledge base to slowly build up new explanations (Glaser & Strauss, 1967). This was simplified by the joint interpretive repertoire (Alvesson & Skjöldberg, 2000), which enabled a careful construction of empirical material to problematize a target theory by the two most involved researches – myself with a deep knowledge of the Skandia story, and Kallifatides, with a background in academia.

To write the history of the recent past is especially difficult. People are still alive and still working. They are still bound by confidentiality agreements. We cannot read other people's thoughts either. Moreover, the interviews were carried out a few years after the bid took place. Peoples' memories are subject to lapses as well as rationalisations. The material is based on information that many of the informants were not allowed to give out. Therefore, their anonymity became an important priority.

The guiding principle was to believe in what interviewees were telling us when it came to "facts" such as dates, people and themes for discussions while remaining more sceptical toward their explanations of motives (their own and others). To a large extent, that principle has proven fruitful in establishing a detailed time line of events; to an overwhelming extent, we have been to obtain confirmation from at least two sources on every single item. In the end the richness of the material gathered from interviews made it possible to reconstruct the Skandia-story in such a way that media reporting could more or less be left aside. Thus the final narrative emerged “an inside-story” and not a report of media accounts.

The end result is, no matter the method, a selective interpretation of events, shaped by the questions, theoretical interest, and personal convictions that we as three researchers with different backgrounds brought into the study. I believe what we have written to be truthful even in those parts were we have had to rely on common sense. Being two researches, and in some parts three, has hopefully helped in that validation.

2 The Capio case

The empirical material of the Capio study was based on a combination of public texts and interviews. The public material covered texts published between 1999 and 2006, with a focus on the two-month period September and October 2006. These texts were selected through the database ”Affärsdata”. In total the media coverage included fifty texts. These were compiled from well-known Swedish daily news papers: Dagens Industri, Göteborgs-Posten, Dagens Nyheter, Svenska Dagbladet, the weekly magazines Affärsvärlden and Veckans Affärer, the news agencies TT and Direkt. Foreign media included wire service Reuters and British newspaper Daily Telegraph and Financial Times.

Public material from Capio included annual reports, board statements and public comments related to the bid. Other relevant sources were statements published by the Swedish Securities Council and Swedish Shareholders Association. A handful of analyst reports from investment banks and securities firms were used as reference. During the writing process I shuttled back and forth between the material and theory.

The material was written out as a chronological narrative during July-August 2010. In the autumn I contacted twelve people that had surfaced as involved in the bid process and asked them to read through the text. I asked them to check the material for possible mistakes. I also asked each to add any additional information that might enrich the material and broaden the knowledge base. In total ten people responded. Follow-ups were conducted using either phone or personal meetings, lasting between one and two hours. Written notes were taken and their comments included in the material. The result has been published as a narrative, using a 7000 word-case study “The hostile bid on Capio 2006” (Nachemson-Ekwall, 2012b, unpublished manuscript). In my dissertation here the material has been summarized as a 3500-word account.

3 The Scania case

The Scania study is based solely on publicly available material. It covers the period 1997–2011, with a focus on MAN’s hostile bid during 2006, and Volkswagen’s extended involvement in Scania and MAN during 2006–2007. The relevant companies have been Volvo, MAN, Scania, Porsche, Volkswagen, and Investor.

The empirical material has included a number of media reports, which can be summarized to an initial screening process including at least thousands from papers such as Dagens Nyheter, Svenska Dagbladet, Dagens Industri, Affärsvärlden and Veckans Affärer. Foreign media include wire services Reuters, Bloomberg News and news papers such as Financial Times. Financial Times was screened using www.FT.com for material covering the entire period, 1997–2011.

Foreign media have also been referred to when quoted by the Swedish wire service Direkt, which when possible was checked with the original text. This has resulted in material having been gathered from The Times, The Sunday Times and Daily Telegraph. References by Direkt have included material from German Handelsblatt, WirtschaftsWoche and Motor und Sports. The material also includes a rich array of public information released by the companies involved. This includes stock exchange amendmens, press releases and financial reports.

As the media coverage unfolded I made a time line for relevant events. Early on the case came to reveal a very different pattern as compared to the Skandia case. Scania involved multiple parties, lasted over a decade, and involved a Swedish company with a blockholder and bidding parties from a German governance regime. To understand the press writings I felt it necessary to extend my research with a study of governance systems. As such the narrative was extended to include accounts of German corporate governance practise, takeover rules and societal embeddedness to gain perspective on actions taken from the bidder, and the parallel development in Sweden that might have effects on Scania. This included material from the Swedish Shareholders Association, the Swedish Securities Council, Stock Exchange statements and the Swedish takeover-regulation from the relevant periods. Thus, the Scania study was in the end built around an actor-centred institutional framework, which included a dynamic perspective given the long time period, which was then used as a theoretical tool to move the narrative forward.

There are a number of limitations to the Scania material. Material that has only been published in German has been excluded, as I do not master the language. No interviews with involved parties have been conducted, due to the complexity of the issue.[154] This said, dates have been checked for accuracy with relevant parties and where possible. However, no party have read the full material. Scania was contacted a number of times during the research process but declined the offer to read and comment. Given the dominant role Scania played in the story I concluded that it might not be appropriate to offer other actors the opportunity to read and comment. As such, the material used for the Scania story could remain a pure recounting of public information, nothing else.

It should also be noted that I had previously followed Scania as a journalist with pieces published in various papers during the period.[155] In particular I covered the Scania–MAN bid fight. This can be regarded as both a weakness and strength, depending on the uniqueness of the stories involved. The weakness is of course related to my pre-conception of the

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[154] Previous writing by the researcher indicates that if interviews were done they would quickly involve more than a hundred people, and could well end up with a few hundred meetings.

[155] Finanstidningen, Dagens Nyheter, Affärsvärlden, Dagens Industri

material, which naturally limits the scope for presenting material with clear objectivity. The strength is that my own journalistic background, and knowledge of some of the actors[156] involved, increased my scope for critical analysis of the written material. Leaking to the press was, to put it mildly, an integral part of the unfolding of the Scania story. This went for all parties, including investors, investment banks, union representatives, representatives for the different companies and so forth. This applied for Swedish, German and UK-based media alike. However, in the usage of media sources I have tried to treat my own writing as objectively as possible.

The written material was in the end unfolded from the period September 2010 to August 2011. The final narrative is found in the extended case study "Scania, the Market for Corporate Control and the Mandatory Bid Rule", (Nachemson-Ekwall, unpublished manuscript, 2012c). The study includes 46 000 words (100 pages). In the dissertation the final Scania manuscript is presented in a shortened version, limited to 8 000 words.

4 The revision of the Swedish takeover rules

The gathering of empirical material started already in early 2007 and continued to July 2011. Material was compiled from open sources such as takeover regulation in the EU (The Takeover Directive), the Winter Report, takeover regulations in the UK, Germany, Finland, Denmark and Norway. I read reports by the EU High Level Group of legal experts. I read a number of government reports, including material published by the Ministry of Justice as far back as the 1980s. This includes legal documents, government bills and proposals dealing with company law, stock market regulation, and takeover regulation. I also drew on work conducted by legal experts related to, in different positions, the Eu-

[156] This would include having to carry out interviews with most of the involved actors from the Swedish parties, and also contacts with representatives of MAN.

ropean Commission.[157] To broaden the perspective of takeover regulation I read relevant parts of the Swedish Companies Act. I also choose to include aspects of the Corporate Governance Codes developed in UK, Denmark, Germany, Finland, Norway and Sweden.

In the actual work with the Swedish Takeover regulation and the amendments done in 2009 I drew on legal experts within the Swedish community. This includes work done by Professor Daniel Stattin, Uppsala University. Stattin's book on Swedish Takeovers (2009) has been especially helpful in its analytical approach to comparing the Swedish takeover regulation with the British and the EU Directive. I have also draw on various works by Rolf Skog, guest professor at Gothenburg University, executive director of the Swedish Securities Council and member of the Commission's European Company Law Experts.

Ahead of working with the Takeover regulation 2009 I also contacted four actors, all with legal background and perceived to be experts in the area, to ask their opinion on the regulation. Three of the interviews were carried out through personal meetings and one by phone, during the spring and the autumn of 2010. I presented two open-ended questions: which changes were the most interesting from your perspective? And, "Is there anything that you wish had been included?" The interviews were transcribed and used as background when pursuing the analysis of the regulations, both as regards to the legal content and application to specific takeover cases.[158]

Thus the account of the takeover regulation came to resemble, just like the empirical work with the company case studies, a detective's work continuously going back and forth between the case studies, legal documents, academic texts and material from the Securities Association.

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[157] These experts included Professors Jaap Winter (Netherlands), Eddy Wymeersch (Belgium), Klaus Hopt (Germany) & Jesper Lou Hansen (Denmark).

[158] The Swedish Takeover Rules are written in such a way that it is not possible to know which case an amendment relates to. The work process lacks transparency: there are no public documents on the working process. What remains is to use a mixture of common sense and questioning parties that have been involved in the process of rewriting the rules.

5 Amendments to the takeover rules of 2009

This is a summary of the amendments to the NBK Takeover Rules of 2009. Its primary source is the press release issued by Näringslivets Börskommitte (NBK), 16 March 2009. Chairman Lars Otterbeck, Secretary Rolf Skog.

1. Actions By Bidding Party

(NBK II.1, II.2) More stringent requirements for "pre-announcements"

From the press release: "The rule clarifies that, in principle, no person may publicly announce the mere intention to make (or that they are considering making) a public takeover bid…" Thus, indicative bids are not permitted unless the Securities Council has given its approval. However, in certain circumstances the council is permitted to issue a clarifying announcement in order to address the imbalance in information in cases where a potential bidder knows, or has reason to suspect, that information on an offer has been leaked or will be leaked in the target.

Comment: When France Telecom's interest in acquiring TeliaSonera was leaked to the market and commented upon by France Telecom, it was unclear if a proper bid was presented or not. (June 2008)

(NBK II.4; II.5) More stringent rules for the withdrawal of bids

From the press release: "It is clearly stated that it is not normally permissible to withdraw an offer that has been made on grounds that the target company Board has recommended that shareholders should not accept the bid." The main rule is that a bidder is bound by its offer.

Comment: When Old Mutual presented its bid on 2 September it was conditioned of a positive recommendation from the Skandia board no later than 15 September.

(NBK II.4, II.5) Limits on the right to change an already presented offer

From the press release: "The new rules clarify that an offer which has been tendered may be changed only in a manner which makes it more favourable for the shareholders… an offer can be changed only when at least two weeks of the period during which an acceptance may be proffered has elapsed." The two-week period is calculated from the time at which the change was announced.

Comment: When US internet-service provider AOL bid on Tradedoubler, it was unclear if the condition of 90 per cent acceptance might be waived or not. When AOL did not receive 90 per cent it walked away.

(NBK II.8) Obligations of shareholders following acceptance

From the press release: "If for example the total acceptance period is more than 10 weeks, a shareholder who has accepted the offer is entitled to withdraw an acceptance that has already been made, as of the eleventh week".

Comment: During the final stage of the Skandia-bid, Old Mutual's investment banks Deutsche Bank and Merrill Lynch tried to pressure hedge funds not to withdraw their shares during the prolonged period.

(NBK II.22) Rules on bidders obligation to announce outcome of bid

From the press release: "The bidder shall as quickly as possible compile the number of accepts to the bid and announce the outcome publicly..."

Comment: Old Mutual speculated openly about acceptance rate from Skandia shareholders (Autumn, 2005)

2. Actions taken by the Target Board

(NBK II.11) Requirements for independence when issuing a fairness opinion

From the press release: "The expert commissioned to produce a ("fairness opinion") must have an independent status in relation to the bidder. This means, for example, that payment for the statement of opinion may not involve a "success fee".

Comment: In Skandia Morgan Stanley prepared a fairness opinion while at the same time it was enrolled by the board and entitled to receive a success fee reflecting the value of a bid. In July 2005 it was decided that the opinion was not going to be published. Still in October, Old Mutual asked Aktiemarknadsnamnden for support in forcing the Skandia board to make it public. The issue also appeared in Capio, in the autumn 2006, when Morgan Stanley prepared a fairness opinion while at the same time receiving a fee based on the success of a bid on Capio.

(NBK II.17) Clearer rules for the role played by the target company board

From the press release: "The board has a central role in the bid process and shall act in the interest of the shareholders…The Board may not act in its own interest or allow it to be swayed by the interest of one shareholders or a limited number of shareholders. If there is more than one bidder the board may not favour any of them."[159]

Comment: In Skandia the chairman of the Board put much emphasis on the view of a limited number of investors, and in doing that made many of the other board members feel that the chairman tried to pressure them into moving a certain direction. (2005)

(NBK II.18) Conflicts of interest within the board of the target company

From the press release: "A director of the board or a CEO of a target company might not participate in the preparatory matters of a bid, if he or she has common interest with the bidding party that might contradict the interest of the shareholders. An example of this is any case when a director is also an owner in the bidding company."

Comment: When private equity firm EQT bid for Q-Med the main owner and CEO Bengt Ågerup participated in the bidding consortium. (November, 2008): In Capio both the chairman Roger Holtback and the previous CEO Per Båtelson had connections to the bidding consortium Opica.

(NBK II.19) The target board's obligation to present its opinion on the bid

From the press release: "It is important that the target board express its opinion…which should be done no later than two weeks before the bid expires."[160]

Comment: Relates to the importance of the board stating its opinion, even if the board is split, as in Skandia. (2005)

(NBK II.20) The target company's obligation to participate in due diligence

From the press release: "The Board shall assure that the due diligence is carried out as quickly as possible so as not to disturb the daily business of the target company."

Comment: The Skandia board had difficulty both with deciding on the due diligence process in May 2005 and coping with the length the due diligence process was to be carried out. The work ended up disturbing management and business activities. (2005)

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[159] Rule II.17 states that "The board of the target company shall in questions related to the bid act in the interest of the shareholders", which is clearer than what was stated in the press release. See next chapter.

[160] Notably the text from the press release is very unclear and does not reflect the meaning of the final NBK rules.

3. Technical Issues

(NBK II.7) More stringent rules regarding the acceptance period

From the press release: “The acceptance period for a takeover bid is not less than three weeks and not more than 10 weeks…the total acceptance period may not exceed 3 months...if subject to approval by a public authority, the acceptance period may not exceed 9 months.”

Comment: Old Mutual’s bid was prolonged a number of times, and the actual period from the prospectus becoming public to the last closing on 14 March 2006 was 24 weeks.

(NBK II.14) Rules limiting rights to make deals outside the public offer

From the press release: “Given equal treatment of shareholders, if a bidding party during a six month period following the offer or outside the offer, buys more than 10 percent of the shares in the target company in cash or in stocks, it follows that all other shareholders included in the offer shall be offered an equivalent alternative.”

Comment: Before Borsa Dubai put fourth its public bid on the stock exchange OMX Holding, it made a partial offer which included a price guarantee, not present in the announced bid. (July 2006)

(NBK II.15) More stringent rules for the withdrawal of bids

From the press release: “The ability to present a bid conditioned on clauses that facilitate withdrawal is very limited… This includes conditions upon a positive recommendation from the board of directors.”

Comment: Old Mutual wished that the bid on Skandia be conditioned on board acceptance. (2005)

(NBK II.15) The right for a bidder to return and buy shares in the market

From the press release: ”Today a bidder may return to the market after nine month after a bid has expired and pay a higher price for shares without offering incumbent shareholders compensation. The suggestion is that the period shall be adjusted to the British rules limiting the time to six month”.

Comment: Adjustment to British rules.

(NBK II.17) Share classes

From the press release: “The suggestion implies stronger requirements concerning different prices offered for different classes of shares.” Where there are shares of different classes in the target, as a general rule the same form of consideration must be offered for those shares, regardless of class. Thus, a bidder cannot offer shares to holders of a particular class of shares and cash to holders of another. If the differences in share class apply only to voting rights attached to the share and only one class of share is made available for trade on the stock market, the same terms must be offered for all shares. The bidder can apply to the council to be permitted to offer different prices for the different share classes if:

- Liquidity in the share class concerned is sufficient to provide a fair price indicator;
- Share price differences are not merely temporary; and
- Share prices are not attributable to the demand of merely one or a few buyers.

Comment: When holding company Kinnevik sold it's A shares, with multiple voting powers, in Invik to Icelandic Milestone it received a premium over the price of the B shares. (April 2007)

(NBK II.24) Limits for bidder to return with a new bid

From the press release: ”A bidder that fails and does not fulfil the offer is not allowed under the new rules to return with a new bid within one year. This also applies if the bidder retracts its offer.”

Comment: General addition, in line with the fundamental principle that public takeover offers may not impede the target's business for longer than is reasonable.

4. Other Amendments

Statutory Merger

A statutory merger implies a merger between two companies where two companies are either combined in a new structure or one company is absorbed by the other company. This might be preferable to a bid since it only requires the approval of a two-thirds shareholder majority at a general meeting to gain 100 per cent. The question of statutory merger has been regulated in the Swedish Company’s Act Ch. 14, in accordance to the EU Merger directive 1994.[161] However, in many listed companies, bidding parties used it to circumvent the minority 90 per cent squeeze-out rule – with the bidder forcing through a cash-bid at a shareholders meeting. In Sweden this possibility was used during the early years after the millennium in cases that were brought to the attention of the Swedish Securities Council,[162] and became standard

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[161] EU Directive 78/855/EEG (*Sw:* “Fusionsdirektivet”) (SFS 1994:802)

[162] *Sw:* “Fusion Inititativuttalande” (AMN 2004:23): “Fusion Realia Wilkinson” (AMN 2005:02).

procedure (Nachemson-Ekwall, December 8, 2004, Affärsvärlden). On 1 July 2007 the procedure was stopped and new regulation was implemented on 1 January 2009 (Ministry of Justice, proposition 2007/08:155). Since then half of the merger value must be paid in shares for the merger rule to be applicable, and the bidder may not vote for its shares at the shareholders' meeting of the company being absorbed, where two-thirds majority is proposed.

Comment: It was not until the Skandia case that it became clear how the Forced Merger Rule was misused also in larger companies, and it was this that stopped it. It was used for the last time when Nordica Capital, through the vehicle Opica, bid on Capio 2006.[163]

Mandatory Bid. Suggestion that a new level for mandatory bid be implemented at 50 per cent control of shares or votes

The question of a Mandatory Bid Rule as brought forth in the EU Takeover Directive has not been included in the NBK Takeover Rules but rather addressed legally in LUA. In 2009 The Commerce Stock Exchange Committee, NBK sent a letter to the Swedish Ministry of Justice to suggest the implementation of another level stipulating a mandatory bid at 50 per cent in addition to the 30 per cent level present since 2003. [164]

Comment: German vehicle producer Volkswagen bought the Wallenberg group's shareholding in Scania in 2008 and took control of 37.7 per cent of shares and 68.6 per cent of votes without being obliged to bid for all shares. (March 20).

[163] In the offer Opica restricted its obligation to fulfil the 90 per cent minority rights rule to force through a merger even if the level of acceptance came in lower, i.e. only at above the 66 per cent level (Press release Nordic Capital 20060901).

[164] *Sw:* "Hemställan till Justitiedepartement om ändring av Lagen för budplikt", NBK September 9, 2009.

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