703:The Law of Europe: A Grand Tour

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Faculty Biographies

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Martin W. Hopkins

Martin W. Hopkins is a partner with Eversheds in Birminham, England. Mr. Hopkins and five colleagues were asked to establish a pure employment and labour law practice in Eversheds' Birmingham office. That practice has grown to 34 lawyers and advisers and is part of Europe's largest team of employment and labour lawyers. He is currently director of business development for all Eversheds' employment and labour lawyers in Europe.

Mr. Hopkins advises mainly international employers on a wide variety of labour law issues including employment implications of international mergers and acquisitions, major reductions in force and senior executive severances. He has advised more than 60 U.S. high tech companies on their set up in the UK and on day to day HR activities. He speaks regularly to groups of HR strategists and corporate counsel on a vast range of issues impacting the workplace. He is a regular speaker in North America.

Eversheds has firm wide pro bono and community volunteering policies in place. This does not just include fund raising but also includes devoting staff time, energies, and talents to organisations and projects that enhance the wealth and prosperity of local communities.

Mr. Hopkins studied at Coventry University and at the College of Law in Guildford.

Laura M. Owen

Laura M. Owen is director, legal affairs at Cisco Systems, Inc., supporting worldwide human resources and work place resources ("WPR"). In this role, she advises on all HR and WPR-related legal issues including litigation and arbitrations globally. In addition, she is responsible for retaining and managing outside counsel worldwide to support HR and WPR.

Ms. Owen joined Cisco from Women.com, where she served as vice president, human resources prior to Women.com's acquisition by iVillage. Prior to that, she worked in the employment law group at Cooley, Godward, where she handled a wide range of counseling and litigation matters for an extensive group of clients. Ms. Owen also worked for United Airlines in the employee relations group where she managed United's interactions with its machinists for the western U.S. region and Canada.

Ms. Owen belongs to the California Bar Association and is admitted to practice before the California Supreme Court, U.S. District Courts of Northern California, and the U.S. Supreme Court. She also serves as a board member for two nonprofit organizations; the Law Foundation of Silicon Valley and The Whistle Stop (child care center for Veterans' Administration employees).

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Ms. Owen received an undergraduate degree from San Francisco State University and her law degree from Santa Clara University.

Kevin C. Randall

Kevin C. Randall is senior counsel – financing & transactions for GE Aircraft Engines in Cincinnati. As such, he is responsible for structuring, negotiating, and documenting GEAE's mergers, acquisitions, and joint ventures, as well as its aircraft financing arrangements and other complex financing structures.

Prior to his appointment to his current position, Mr. Randall was senior counsel – tax affairs with GEAE and was responsible for structuring acquisitions and joint ventures in numerous countries, including the UK, France, Russia, Brazil, India, Taiwan, China, and others. Prior to that, he was a shareholder in the law firm of Johnson & Gibbs in Dallas where he had a transactional tax practice.

Mr. Randall served on the board of directors of Synchrony Communications, an internet start-up, at the height of the internet bubble. He is also involved in the annual fund-raising efforts for the Cincinnati Fine Arts Fund.

Mr. Randall received a BA from Miami University in Oxford, Ohio and is a graduate of the University of Michigan School of Law.

Nicholas R. Sayeedi

Nicholas R. Sayeedi is a legal director at EchoStar Communications Corporation, a Fortune 500 distributor of satellite video, audio, and data programming and consumer electronics products. In addition to co-managing the EchoStar legal department, Mr. Sayeedi oversees EchoStar's international, marketing, employment, and IT legal work, and serves as corporate secretary for all of the company's European offices.

He formerly served as EchoStar's lead securities and M&A attorney.

Prior to joining EchoStar, Mr. Sayeedi was an associate in the corporate and securities department of a large international law firm.

He holds a BA and received his JD from the University of California.

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The Law of Europe: A Grand Tour

"When you look at Europe, do you see a single place or 49 independent countries, each with a different legal system? If your role as legal advisor has you working on European endeavours, you need to understand the law of Europe, taking time to appreciate differences among the legal systems of different countries as well as vis-à-vis the United States. Using case studies, we will explore the range of variations and demonstrate how real life scenarios can play out differently in different jurisdictions. Take away a key resource for a better understanding of the nature and extent of differences and similarities of the law of Europe."

Our Vision

'The Law of Europe: A Grand Tour' is a presentation for corporate counsel who are, or will be required to provide legal advice relating to business activities which impact, either directly or indirectly, on the European states and therefore on European legislation. The presentation will draw examples from three key legal areas: Employment and Labor Law, Corporate Responsibility and Data Privacy. Through practical examples and interactive case studies, attendees will be able to tap into our panel's in depth knowledge and expertise in order to provide clarity to the potentially daunting prospect of the legal framework which exists within the European Union.

Presentation Structure

Our panel will be presenting for 90 minutes. As described above, the session will focus on three practice areas:

- Employment and Labor Law - presented by Martin Hopkins (Eversheds LLP) and Laura Owen (Director, Legal Affairs, Cisco Systems Inc).
- Corporate Responsibility and Mergers & Acquisitions - presented by Michelle Thomas (Eversheds) and Kevin Randall (Senior Counsel, GE Aircraft Engines).
- Data Privacy - presented by Paula Barrett (Eversheds) and Nick Sayeedi (Legal Director, Echostar Communications).

'The Law of Europe'

As part of the presentation we will be providing all attendees with 'The Law of Europe'. This is a definitive and original text commissioned and published by Eversheds. It is an essential starting point for any corporate counsel who is tasked with navigating the legal seas of the European Union.

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EMPLOYMENT AND LABOR LAW

The area of employment and labor law is a perfect example of the basic contention. that throughout the European Union there is much consistency in the compliance framework.

Two particular compliance areas serve to demonstrate that point

Discrimination

Throughout the EU there is now, or soon will be, a high level of consistency in terms of compliance framework. There is an overarching commitment amongst all EU members to harmonise the rights and obligations in the HR space over an extended time frame. In the discrimination area, that general commitment is made specific by the recent Framework Directive which requires all member States that implement a basic and consistent structure of discrimination protection and compliance by 2006.

That European framework will also be very familiar with your system in the US. That said, there are currently, and will continue to be, many subtle but significant variations at an implementation level as between the EU and the US and also within different EU Member States. Additionally, in this area, cultural differences as between different countries will always have an impact upon the way in which discrimination plays out on a day to day basis in individual businesses.

Europe is currently migrating towards compliance with the Framework Directive and for the moment different Member States are at different points on that journey. Their discrimination legislation as at today will reflect a range of historical differences as a consequence of which there is currently quite a good deal of variation from State to State. Not only have countries started their journey towards the 2006 target date from different starting points but they are also moving at different speeds. This therefore means that there is today much variation in the compliance regimes currently in operation across Europe.

Looking at the framework as provided for by the Framework Directive, US lawyers will find the essential structure very similar to that which they know in the US. In simple terms, there are four prohibited behaviours, namely:-

1. Direct discrimination, which you will know as disparate treatment discrimination.
2. Indirect discrimination, which you will know as disparate impact discrimination.
3. Harassment.
4. Victimisation, which you will know as retaliation.

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The characteristics that are protected via the Framework Directive will also be familiar to US lawyers include:-

1. Gender
2. Race
3. Ethnic origin
4. Age
5. Disability
6. Sexual orientation
7. Religion or other similar belief.

The circumstances in which the Framework Directive provides that protection should be available are also familiar and include:-

8. Access of employment and training.
9. Working conditions.
10. Membership of work organisations.
11. Access to Social Security.
12. Access to healthcare and education.
13. Access to cultural activities.

Collective representation

Here again, there is a greater level of similarity of approach throughout the EU than you might expect. It is also an area where many elements of the EU experience are familiar to US lawyers. That said, there are other areas where the differences between the US and EU experience are striking and cause real difficulties in practice.

We have Trades Unions in the EU and their structure, method of operation and attitude is very similar to that which you will be familiar with in the US. You will also, on occasion, find EU Trade Unions just as combative as their US cousins.

An area of contrast in the experience is in the influence that EU Trades Unions are able to extend over individual rights and individual contracts of employment. In many EU countries very high proportions of all employees will be employed on contracts, the terms of which have been negotiated at a collective level by the Trade Union. The best example of this is probably France where less than 10% of the working population are Trade Union members but where over 80%

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of the working population are employed on contracts, the terms of which have been negotiated at a collective level.

Another major contrast between the operation of the Trades Unions in Europe and in the US is in the power that EU Trades Unions have to make law. This is a relatively new EU concept through which the EU Commission will identify an area in which it wants to create new law. Rather than draft that law itself it will delegate the task to "the Social Partners" which is a collection of three separate organisations, namely the European Trade Union Confederation, the Union of Industrial and Employer's Confederations of Europe and the European Centre of Enterprises with Public Participation and of Enterprises of General Economic Interest. In other words, the Commission delegates the task of making new law to Trade Union and employer representative organisations.

This is not merely a theoretical exercise as the Social Partners have already created three new statutes in Europe in the areas of parental leave, part-time work and fixed term contracts. They also have a number of other legislative tasks on their desk today.

Looking at collective representation more generally, the other area which needs to be addressed is that of the Works Council. This is a very common concept in EU and yet almost entirely unheard of in the US.

In simple terms, Works Councils are employee representative bodies set up for the purpose of information, exchange and consultation. Some people have described the Works Council as simply an in-house Trade Union. This is something of an over-simplification but does help to convey a general idea of their objective. Works Councils are a firmly established concept in the EU but are alien to the vast majority of US businesses.

The constitution and operation of the Works Council will vary from country to country within the EU. Currently all countries in the EU other than Ireland, Sweden and the UK already have domestic Works Councils and those three countries will now be obliged to introduce the concept into their countries by 2008 at the latest. In other countries, such as Germany the Works Council has been an established part of the collective framework since the 1920s.

The impact and power of the Works Council will vary from country to country. That said, in a number of EU jurisdictions any significant decisions taken regarding the business and/or the employees who work within it will be void and unenforceable unless the Works Council has been consulted before the decision is taken and implemented. In certain extreme examples no decision can be taken until the Works Council has actually agreed to the proposal under discussion. There are a number of high profile examples of sophisticated businesses which have been forced to unravel strategic and significant business decisions (often regarding plant closures) simply because they did not honour their consultation obligations with the Works Council.

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The background

The Continent of Europe contains 47 independent sovereign countries.

The European Union is a subset of the Continent of Europe and currently contains 15 Member States. In 2004 that number will rise to 25 Member States.

One of the features of the EU is that Member States commit to harmonise their legal systems over an extended period so as to deliver the social and political objectives of the EU.

Accepted logic has until now provided that the each separate country in the EU has a legal system which is completely different and that similarities as between those countries is the exception rather than the rule.

Our premise is that there is much greater similarity of approach across EU Member States than has previously been recognised.

Using examples and/or case studies we will seek describe that similarity, demonstrating as we do so:

1. Areas where the EU approach either differs from or mirrors the US system, and

2. Areas where despite a high level of similarity within the EU there are nevertheless differences of detail and/or application that lie in wait to destabilise the unwary.

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CORPORATE

The presentation will focus on the key issues for US businesses considering a move to or within Europe and the legal structure and rules likely to influence the operation of the business thereafter.

The move to or within Europe:

The presentation will focus briefly on European enlargement and the implications of this as a factor influencing the location and migration of business within Europe (see European Lawyer Article 2003 by Michelle Thomas and Zannah Woods-Scawen titled "Should we stay or should we go"). There will be a brief consideration of current trends to out source or move certain business operations to lower cost centers within Europe and the likelihood of certain companies moving in the event that these cost centers lose their attraction.

The presentation will then explain some of the key issues for US corporates to consider if the move into, or expansion within, Europe is to be by way of acquisition (see European Lawyer Article 2001 titled "Acquiring in the UK" by Michelle Thomas). It will touch briefly on labor law and commercial contracts issues and how these, by way of an example, are treated differently.

The Law of Europe and its impact on US business

We will discuss, once a business is in Europe, the key implications of "European Law" on operating a business in Europe. We will discuss the harmonisation and convergence of laws within Europe and consider the cost implications of the recent changes for business (See Eversheds: The Law of Europe)

In addition, and in light of the recent concern over corporate governance in the US and the procedures for reporting compliance with the same, we will briefly outline the corporate governance structure in Europe and compare this to the US. We will then answer some frequently asked questions about the compliance regime in Europe and the extent of Sarbannes-Oxley on this.

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DATA PROTECTION

1. INTRODUCTION

1.1 As the European Union began to grow in terms of the number of member states and the volume of business and communication between those states, the European Commission became concerned about the ways in which information about individuals was being processed and transferred not only between states within the European Union but also from member states to third party countries. In response to these concerns, the Commission issued its Data Protection Directive in 1995. The aim of this Directive was to ensure that individuals would be guaranteed a certain level of privacy in relation to their personal data across all EU states. Each member state has implemented its own legislation to comply with the requirements laid down in the Directive.

1.2 US companies can become involved in European Data Protection in broadly three situations:

1.2.1 Where an individuals personal information (even that of a US citizen) is processed by or on behalf of that US Company using equipment located in the EEA;

1.2.2 Where the US company has an office, branch or agency in the EEA or acquires a corporate entity within the EEA which is processing individuals personal information;

1.2.3 Where the US company receives an individual's personal information from a business in the EU then it will find increasingly that it is asked to provide adequate protection, equivalent to the Directive, to that data via contract or through a safe harbour registration (explained below).

1.3 Where this occurs the US Company needs to become familiar with the Directive and the implementation of it in the member states in which the processing of the personal information is taking place or from which it is exported.

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2. THE DATA PROTECTION DIRECTIVE

2.1 The EU Directive, issued by the European Commission in 1995, provided that all member states must introduce national legislation which complied with the requirements of the Directive by October 1998. Most have done so, but not all. The Directive restricted the way that personal data could be collected and processed. It also provided that processors of the data must register with the relevant supervisory authority. The Directive provided for restrictions on the transfer of personal data within the EEA and from the EEA to other non-EEA countries.

2.2 The essence of the Directive is that the personal data must:

2.2.1 be processed fairly. "Processing" includes the holding of data, as well as amending, deleting, accessing, review and transferring;

2.2.2 be collected for specified, explicit and legitimate purposes;

2.2.3 be adequate, relevant and not excessive;

2.2.4 be accurate and kept up to date. Data which is not adequate or up to date should be erased or rectified;

2.2.5 be kept in a form which permits identification of the individual for no longer than is necessary;

2.2.6 be kept securely; and

2.2.7 not be transferred to any territory outside of the EEA where there is not adequate protection for the rights and freedoms of the individuals in relation to the processing of the data about them carried out there.

2.3 In addition, personal data may only be processed if particular conditions are satisfied. These include:

2.3.1 the individual consents to it being processed;

2.3.2 the processing is necessary for the performance of a contract which the individual is party to;

2.3.3 the processing is necessary to satisfy a legal requirement;

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2.3.4 the processing is required to protect the vital interests of the individual.

2.4 Except where further restrictive conditions are satisfied in addition, it is prohibited to process personal data revealing racial or ethnic origin, political opinions, religious beliefs, trade-union membership and data concerning health or sex life. These additional conditions include where the individual has given his explicit consent or where the processing is necessary to comply with employment law obligations in so far a national law authorises it and provides adequate safeguards for the processing of such data.

2.5 The Directive also gives the individual about whom data is processed certain rights. These include the right to have the information held about them corrected or blocked, to object to direct marketing, and to have access to the data held about them. For example, in the UK, an individual may make a 'subject access' request to an organisation which he or she believes holds data about them. The recipient organisation, assuming it controls the processing of that information, is then under an obligation to conduct a reasonable search of its records and provide the person making the request with all data that it holds about that person which doesn't fall within very the limited exemptions to this access right.

3. PERSONAL DATA

3.1 The concept of "personal data" pervades all areas of EU data protection regulation. As we have discussed, the EU Directive and subsequent member state legislation restricts the collection and processing of "personal data". The EU Directive broadly defines "personal data" as "any information relating to an identified or identifiable natural person". In practical terms this means any data from which a person can be identified, directly or indirectly. The data must, therefore, make reference to the individual's name, an identification number or one or more aspects of the person's physical, physiological, mental, economic, cultural or social identity. It is important to note however that the definition of personal data has been expanded in some member states. The UK implemented the Directive by passing the Data Protection Act 1998. This Act expanded the type of data that was subject to protection by including not only data that contain 'information' relating to the individual, but also which included any "expression of opinion" about the individual. In other Member States, for example Belgium, in principle all data which can be linked to an individual, are regarded as personal even if the data are processed by someone who cannot make that link. The laws in Austria,

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Italy and Luxembourg extend the concept of data subject to legal persons e.g. companies.

4. DEALING WITH COMPLIANCE

Where US companies come into contact with European data protection they need to adopt a compliance programme.

4.1 Currently, the US is not deemed by the EC Commission to provide adequate protection for personal data and so the restriction on transfer outside of the EEA in the Directive can cause compliance problems. Where the US company will receive "personal data" from a country within the EU (whether that's from an office located there, a sister company or a third party), there are a number of compliance options, which include:

4.1.1 Firstly, they can seek to enter into a contract with the Data Provider incorporating the standard contractual terms approved for these purposes by the Commission.

4.1.2 If the Data Provider is a sister company or branch office then its could put in place a legally binding group policy though this would need individual approval of it terms from the Commission.

4.1.3 They could investigate whether the information can be anonymised before transfer so as to no longer qualify as "personal data"

4.1.4 A further alternative is for the US company to register under the US safe harbour scheme agreed between the US government and the Commission. By doing so the US company is undertaking to comply with seven principles of protection which broadly reflect the principles in the Directive. The principles are as follows:

(a) Notice - the US company receiving the information must notify the individuals concerned. They must confirm the purpose of collecting the data and the kinds of organisations to which it is going to disclose the data.

(b) Choice - individuals must be allowed to choose whether the US company can disclose their data to other third party organisations.

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Individuals are also allowed to request that their data is not used for purposes other than that for which the data was collected.

(c) Onward Transfer - this provides that the US company may only forward information to a third party organisation if it ensures that the third party will provide the same level of protection as provided under the safe harbour principles.

(d) Access - US companies must provide the individual with access to the data and allow them to correct any incorrect information. This is not required if the burden of providing access is greater than the risks associated with holding erroneous information.

(e) Security - companies must take reasonable measures to protect the personal information from unauthorised access or alteration.

(f) Data Integrity - procedures must be in place to keep the information accurate and reliable.

(g) Enforcement - the company must have in place a system for investigating and resolving individuals' complaints and disputes. The company must also verify that it is complying with the safe harbour principles by way of an independent verification body or by conducting an annual self assessment.

4.2 Where the US company has a corporate entity in a particular member state, it should register that entity with that member state's data authority, for example in the UK, the company should register with the Office of the Information Commissioner. That corporate entity will be required to comply in full, with the local data protection legislation.

5. SANCTIONS FOR NON-COMPLIANCE

5.1 The consequences of being found in breach of the relevant data protection regulation in a member state can be serious, and may include:

5.1.1 Criminal Liability - for example, under the UK Data Protection Act there are circumstances where the Data Controller may be subject to criminal sanction, for example, if they process information without making a proper notification

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to the data protection authority (the Office of the Information Commissioner). Such omission may result in a potentially unlimited fine. In Sweden, the penalties include fines and for the most severe cases, imprisonment for up to two years. These sanctions, obviously, can not be taken seriously enough. The liability for such crimes may attach to the corporate entity and/or, under UK law, any director, manager, secretary or similar officer of the company where the offence has been committed with that individual's consent or neglect. A reason for this personal liability is to ensure that senior officers do not ignore the Data Protection regulations.

5.1.2 Civil Liability - this may arise in circumstances whereby the individual believes his data is being processed without his consent, in a way that causes or is likely to cause substantial damage or distress. If the company cannot prove that it had taken reasonable care to comply with the Data Protection provisions, it may be liable for a fine.

There was recently such a claim in the UK where a local government authority used a child's picture in a publicity brochure without her consent. The parents requested that the brochure was withdrawn. After promising to do this, but continuing to distribute the brochure, the authority was requested to pay the child $78,000.

5.1.3 Commercial Considerations - aside from potential criminal and civil liability, there are other ramifications, for example, the company may be ordered to forfeit, erase or destroy the data held. This would obviously have a severe adverse impact on the company's ability to operate efficiently, or indeed, at all.

6. CONCLUSION

6.1 In the age of modern technology, we are all accustomed to transferring vast amounts of information at the push of a button. It is easy to do and has become second nature to all of us in all types of business. The EU and the member states within it are committed to affording a high degree of data privacy to its individuals. If a company from outside the EU wishes to receive or exchange information with member states it must be aware of, and comply with, the protection provided to the individuals who are the subject of data they wish to acquire.

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ACQUIRING IN THE UK

Eversheds Summary Paper

There are a range of issues to be considered when acquiring the business of, or shares in, a UK company. For the purposes of this note, references to acquisitions of, or from, UK companies are to companies incorporated in England and Wales. Many of the issues will be similar to those which arise on US acquisitions although their treatment under the UK system will be different. The aim of this note is to highlight those issues which you need to ensure are considered at the outset – almost as a check list – which, if relevant, will impact on the timing and structure of the acquisition. If you have any questions then please call us. Our contact details are set out at the end of this note.

1. Is this a share or asset acquisition?

This note does not attempt to explain the differences between share and asset or business acquisitions. In addition to other factors, US and UK tax considerations will be a key issue in determining which route is taken. If you require advice on structuring the form of acquisition, then please consult us. The following basic principles may, however, be useful to note.

Share acquisition

If your client is acquiring shares in a UK company, the first question to ask is whether the Company is a private limited company (identifiable by the words "Limited" or "Ltd" after its name) or a public limited company (identifiable either by those words or "PLC" after its name) as this will have a bearing on a number of considerations which are highlighted in this note.

The mechanics for the transfer of shares are relatively simple. Shares are transferred to a purchaser by means of a written stock transfer form. The form must be stamped, if appropriate, and must be signed by the seller. For further details on stamping of documents, see paragraph 5 below. The transfer will (following the payment of stamp duty) be registered in the company books of the target company and a share certificate issued to the purchaser as evidence of

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ownership. The process is broadly the same in respect of the transfer of shares in a plc, however, the process will vary if the shares are listed and/or held in uncertificated form (on CREST).

Asset acquisition

If assets are to be purchased then only those identified assets and liabilities which the purchaser has contractually agreed to acquire will be transferred. Hence, the purchaser may "cherry pick" assets and associated liabilities.

The important point to note is that, in contrast to a share acquisition, an asset acquisition will not necessarily constitute the purchase of a "going concern". This will be of particular relevance in respect of sales tax and employee liabilities especially if certain contracts or trading arrangements are excluded from the sale. These points are discussed in paragraphs 3 and 4 respectively.

In addition, certain assets will need to be separately identified and transferred pursuant to specific forms of transfer. Real property, for example, must be transferred by conveyance or assignment.

Consents and approvals are also likely to be more significant on an asset purchase since there will be a change of ownership of the individual assets. The consent of customers, suppliers, landlords and others in respect of the assignment or novation of existing contracts will be relevant in this context.

2. Regulatory issues

If your client is acquiring shares, there are a number of regulatory checks to make. These become more onerous if the company is public (as opposed to private) and furthermore if the shares in the public company are listed (registered) on a stock exchange.

Takeover Code

Any takeover offer for a public company, whether or not its shares are listed, will be regulated by the non-statutory City Code on Takeovers and Mergers ("the Code") as published by the Takeover Panel. As a general rule the Code will not apply to takeover offers for private companies unless the private company has, in the previous 10 years, listed its shares, had its share price published, had its shares subject to a marketing arrangement or filed a public prospectus. If the public company's shares are not listed nor held by a large or disparate

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shareholder base, it may be possible to obtain a waiver from the Takeover Panel permitting the takeover to be conducted outside the ambit of the Code.

The Code contains detailed provisions for the timing and nature of takeover offers as well as provisions designed to prevent a potential target company from taking steps to frustrate an offer without the approval of its shareholders. The Code also provides for offers to be made by offer document with a form of acceptance rather than executed contracts.

If the target is a listed public company, the Substantial Acquisition Rules ("SARs"), as appended to the Code, will also apply in the period leading up to the offer for the share capital of the target. In simple terms, the SARs restrict the speed with which a person may increase its holding in a listed company prior to a formal offer as well as setting out the required disclosures for stake building.

Financial Services and Markets Act 2000

The Financial Services and Markets Act 2000 ("the Act") regulates the conduct of "regulated activity". This is broadly defined to include the buying, selling or subscribing of securities (including shares) or offering, making or agreeing to do the same. Anyone carrying out regulated activities must be authorised under the Act. Failure to comply with the Act may constitute a criminal offence and may invalidate the relevant transaction.

The most important provisions of the Act which are likely to be relevant on a share acquisition of a UK company (whether public or private) are as follows:

- *financial promotion restriction*

A person may not in the course of business communicate an invitation or inducement to engage in investment activity unless the person is an authorised person or it falls within a specific exemption. This will include documents inviting a sale/purchase of a company's securities including, for example, an offer document for a company's shares. The restriction also applies to a communication originating outside the United Kingdom if it is capable of having effect in the United Kingdom. Failure to comply with this regulation may constitute a criminal offence and could render the resulting agreement unforceable.

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- *regulation of unsolicited real time communication*

Any invitation or inducement to engage in investment business made during or as a consequence of communication by telephone, by video conference or in person, without invitation, to a person in the UK or from the UK to a person elsewhere is prohibited.

Generally an acquisition of business assets will fall outside the Act since it will not fall within the definition of "investments". The only exception to this will be where the disposal of assets includes a disposal of shares.

The Companies Act 1985

The following are a summary of the common issues which arise under the Companies Act 1985 on an acquisition of shares.

Acquisition of minority interests

S428-430 of the Companies Act 1985 address the acquisition of minority shareholder interests. Where a bidder acquires 90% of a target's shares through acceptances of its offer it can, subject to the satisfaction of certain conditions, compulsorily purchase ("squeeze out") the remaining 10%. The provision applies equally to private and public companies. The important point to note is that these "squeeze out" powers will only be available if an offer has been made for the entire issued share capital on equal terms to all shareholders of the same class. If "sweetners" are offered to some, but not all, shareholders the bidder will not be able to take advantage of these provisions.

Financial assistance

On any acquisition of a UK company's shares (whether public or private) it will be important to check the transaction structure for any possible unlawful financial assistance.

Briefly, the Companies Act 1985 prohibits a target company or its UK subsidiary from giving "financial assistance" for the purpose of the purchase of the target company's shares. Financial assistance is broadly defined to include assistance given by way of gift, guarantee, security, indemnity or loan or by any other form of financial assistance whereby the company's net assets are reduced to a material extent (or which has no net assets). There are certain exemptions from the prohibition on financial assistance including, in the case of private companies, the possibility to follow a "whitewash" procedure to approve the assistance. It is important to note that the

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whitewash procedure is not available for public companies. The penalty for breaching the financial assistance rules is a fine or imprisonment or both.

Proposals to relax the financial assistance prohibitions for public companies and to remove them entirely for private companies are currently being considered. These proposals are not as yet incorporated into UK law.

Notification of interests

Part VI of the Companies Act 1985 requires the notification of certain interests in shares of a public company whether or not those shares are listed. In broad terms, a shareholder/purchaser who acquires a 3% interest in a public company's share capital is required to formally notify the company. Further acquisitions will also require disclosure. These provisions do not apply to private companies.

Public Offers of Securities Regulations 1995 ("POS Regulations")

The POS Regulations apply where securities (defined to include shares and loan notes) are "offered to the public in the United Kingdom for the first time". In these circumstances the offeror must publish a prospectus containing detailed information as specified by the POS Regulations. The publication of a prospectus will clearly add to both the cost and timing of a transaction. Loan notes are, for tax purposes, currently an attractive form of consideration on share sales and are commonly offered as an alternate to cash. It is not uncommon to see "mix and match" offers pursuant to which the bidder offers selling shareholders the option to take cash, shares or loan notes or a combination (a "mix and match") of all three. The tax advantages associated with the issue of loan notes as consideration on a share acquisition are set out in paragraph 4 below. If loan notes or shares are to be offered, a consideration of the POS Regulations will be key.

There are a number of important exemptions where a prospectus need not be published which may be relevant including:

- where securities are offered to no more than 50 persons;
- where securities are offered in connection with a "takeover offer" (defined in the Regulations but broadly meaning an offer for the entire issued share capital on equal terms to all shareholders); and

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- where securities are offered to persons who ordinary activities involve them in buying, selling or managing investments.

The Listing Rules

Whenever a UK listed company is involved in an acquisition or disposal of shares or assets the provisions of the Listing Rules must be considered and their impact on timing evaluated.

Chapter 10 of the Listing Rules sets out the requirements for transactions, principally acquisitions and disposals, by a listed company. The chapter classifies such transactions according to size by reference to a number of percentage ratios. Each class of transaction must comply with a different set of announcement, notification and consent requirements. On major acquisitions ("Class 1"), for example, the listed company will be required to send an explanatory circular to shareholders (containing certain prescribed information about the Plc and the assets or shares to be disposed of), to obtain shareholder approval of the transaction and to make an announcement to the Company Announcements Office.

If the purchaser itself has a listing in the UK, it will also be obliged to conform with the obligations and disclosure requirements of the Listing Rules.

Merger clearance

The UK or EU merger control rules may apply. If the acquisition is one where two or more enterprises (at least one of which carries on business in the UK or is under the control of a company incorporated in the UK) are brought under a common control or ownership and:

(i) as a result of the merger a market share of 25% or more in the supply or consumption of goods or services in the UK is created or enhanced; or

(ii) the value of the targets gross worldwide assets exceeds GB £70m,

the UK Office of Fair Trading and the Competition Commission have the power to consider the effects that such an acquisition may have on the relevant market and the public interest. Whilst pre-notification to the regulatory authorities is not mandatory where the above criteria is fulfilled, it is advisable.

The above criteria will also apply to an acquisition of assets if the acquisition is deemed to constitute an acquisition of "an enterprise". The relevant assets must constitute the activities of a business but would generally include the transfer of goodwill and commercial contracts.

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If the acquisition is deemed to have a community dimension, European Merger Control Regulations require the acquisition to be notified to the European Commission for prior approval. Whether an acquisition has a community dimension is dependent on the level of its worldwide turnover, EU turnover, as well as this turnover within individual member states. In the event that an acquisition is deemed to have a European dimension, European Merger Control Regulations will override UK merger control requirements.

In the event that the target carries on business within more than one EU member state, it is generally advisable to obtain clearance through European Merger Control Regulations rather than through the relevant local jurisdictions.

3. Other relevant issues

In addition to the specific regulatory regimes set out above, the following matters will also be relevant.

Shareholder arrangements

It is common for the articles of association (bye-laws) of a private company to restrict the transfer of shares to non-members, for example, by providing pre-emption rights in favour of existing shareholders. These restrictions may also be set out, and are often mirrored, in a shareholders agreement. The company's articles together with any agreements between members should be reviewed at an early stage particularly where not all the share capital is being acquired.

Listed companies are not generally permitted to impose restrictions on the transfer of shares which are publicly quoted.

Grants and licences

Conditions are often attached to licences which must be reviewed, particularly in respect of possible revocation on a "change of control" of the licence holder. Both share and business purchases can constitute a change of control for these purposes. Licences will be of particular relevance in the banking, insurance and telecommunications sector. Certain areas of the UK encourage new business by way of grants and a check should be made to determine whether any consents in the context of a sale will be required.

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Asset sales and TUPE

"TUPE" is an abbreviation of the *Transfer of Undertakings (Protection of Employment) Regulations 1981* which derive from the *Acquired Rights Directive 77/187.* The purpose of the TUPE Regulations is to protect an employee's employment wherever there is a transfer of an undertaking or business. Note, TUPE does not apply on a share acquisition as the employees will automatically transfer with the Company. The effect of TUPE is to treat certain transfers of assets or businesses as if they were share sales such that the employees transfer with them. The contract of employment will be deemed to transfer from the original employer, the transferor, to the new employer, the transferee.

The practical consequences are that the new employer will be bound to provide the same terms and conditions of employment (save for rights in relation to occupational pensions) as the original employer. Rights under profit related pay or bonuses schemes may also transfer depending on the terms of the schemes. Any pre-existing collective agreements will also transfer. Post termination restrictive covenants will be enforceable against the employee by the new employer in so far as they could have been enforced by the original employer.

Statutory liabilities will also transfer and accordingly the new employer will inherit liability for any breaches by the original employer of employees' rights for example the right not to be unfairly dismissed. All employees transferred will retain continuity of service.

Any dismissal connected with a TUPE transfer will automatically be unfair unless it can be demonstrated there was an "economic, technical or organisational" reason for the dismissal and it was reasonable in the circumstances to dismiss.

Of course, it will always be open to the parties to negotiate the apportionment of liabilities. For example, it may be agreed that, whilst pre-transfer liabilities will automatically transfer under TUPE, the Seller will indemnify the Purchaser in respect of the same.

In addition, the TUPE Regulations impose a requirement on both the transferor and transferee to inform and consult appropriate representatives of the employees affected. These obligations clearly can cause problems where the transaction is still confidential.

The TUPE Regulations are to be revised imminently.

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Environmental issues

There is a sophisticated system of laws in the UK for the protection of the environment. These range from criminal sanctions against pollution to a series of consents and authorisations for waste disposal and other industrial processes. Regulatory control is exercised both at a central and local government level and substantial penalties can be imposed where regulations have been breached.

Whilst liability for breach in essence is directed at the "polluter" it can also apply to those in ownership or occupation of land and hence will be relevant on both a share and asset acquisition. Where a purchaser acquires shares, as opposed to assets, the purchaser will acquire not only the environmental risks associated with the current state of the land or operating assets and processes of the business but also any actual or potential liability arising out of the company's past activities (this would include any claims from third parties).

Directors of UK companies may also be personally liable for breaches of UK law in circumstances where they have acted negligently or in knowing breach of environmental law.

Typically any purchase contract will include detailed warranties and possibly indemnities against environmental liability and damage and an environmental audit may be required.

Property/real estate

On an asset acquisition it will be necessary to provide separately for the transfer of all the property interests of the vendor to the purchaser. These transfer arrangements (including possible consent requirements) will differ depending on whether the land is freehold or leasehold. In addition, land which is registered will require notification of the transfer at the relevant land registry.

Title to land may also be encumbered by mortgages or charges and in some cases property cannot pass until these encumbrances have been cleared or appropriate consents obtained.

4. Tax

The summary below is intended to highlight some of the relevant issues from both a purchaser and vendor perspective.

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Tax and the non-UK purchaser

- *Tax effect of a purchase of UK assets/shares*

Generally, a purchase of shares will result in the purchaser inheriting all of the target company's taxation liabilities whereas a purchase of assets will clearly avoid this. The share purchase agreement will usually incorporate appropriate tax warranties and indemnities to avoid unforeseen tax liabilities having to be borne by the purchaser.

A non UK resident acquiring business assets in the UK will be deemed to have established a branch or a permanent establishment in the UK and its profits attributable to the UK branch will then be subject to UK taxation. An acquisition of shares insulates the non-resident buyer from UK taxation, other than tax paid by the UK target on its profits and any withholding taxes due on interest or dividends received by the buyer.

- *Stamp duty*

Stamp duty (a form of transfer duty) is payable by a purchaser of shares in a UK registered company at the rate of 0.5% of the consideration paid.

On the acquisition of a business, stamp duty may also be payable, depending on the nature of the assets acquired. Broadly, stamp duty will be payable on the value attributable to freehold or leasehold land, fixed plant and equipment, book debts and goodwill, but stamp duty will not be payable on any part of the consideration attributable to loose plant and equipment, stock, intellectual property rights or cash.

Rates of stamp duty vary on an asset purchase. If the total consideration for all assets, whether chargeable to stamp duty or not, exceeds £500,000, the rate of stamp duty will be 4%. Lower rates of stamp duty apply if the total consideration is less than £500,000 (3%) or less than £250,000 (1%). A nil rate will apply where the consideration does not exceed £60,000.

There are various stamp duty saving schemes which can be used to reduce or defer the payment of Stamp Duty.

- *VAT (sales tax)*

VAT is not payable on the sale and purchase of company shares, but will be relevant on a purchase of assets. However, where the assets are purchased as part of an on-going business,

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VAT need not be paid provided the purchaser is registered for VAT in the UK. It will be important, therefore, to determine whether the assets constitute an on-going business.

Tax and the UK vendor

An understanding of the tax position of a UK resident vendor may also assist the purchaser.

Individual tax

- *Capital Gains Tax (CGT)*

An individual or non-corporate UK resident will be liable to pay CGT at the relevant marginal tax rate (usually 40% or 34% for Trustees) on any chargeable gain arising on the sale of shares or capital assets of the relevant business. The chargeable gain is the difference between the sale proceeds and the shareholder's original acquisition price after allowing for any indexation relief and taper relief.

- *Indexation relief*

A vendor who held shares or business assets before 6 April 1998 will be allowed to increase the acquisition price in line with the increase in the Retail Price Index from the date of the relevant acquisition until 6 April 1998.

- *Taper relief*

Taper relief replaced indexation relief for the period of ownership after 6 April 1998 and reduces the chargeable gain for each year that the shares or business assets have been owned since that date. Depending on when the shares or other business assets were first acquired, taper relief can reduce the chargeable gain on unquoted shares or business assets by up to 75%. The rate of reduction is lower for shares which are fully quoted unless the shareholder is an employee of the company in which it holds shares or holds a 5% interest or more.

- *Holdover*

A shareholder may defer all or part of the capital gains tax liability if the payment for the shares is not all in cash. To the extent that payment is received in the form of shares or loan notes (in the prescribed form) issued by the purchasing company, such shareholder may hold over the chargeable gain until those replacement shares or loan notes are disposed of or repaid. In certain circumstances, taper relief will continue to apply, further reducing any chargeable gain.

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Corporate Tax

A company will pay Corporation Tax on any chargeable gain arising on the sale of shares or business assets. The chargeable gain is calculated in a similar way to that for an individual except that taper relief will not apply to chargeable gains made by companies. Indexation relief will, however, apply to the entire period of ownership and not only the period pre-6 April 1998.

With effect for disposals of shares after 1 April 2002,subject to certain detailed criteria being met, the UK grants an exemption from capital gains tax for the disposal of shares by a company, providing that the disposing company has held at least 10% of the issued ordinary share capital of the company whose shares are the subject of the disposal for a period of 12 months during the two years prior to disposal. Correspondingly no tax relief is given for capital losses arising on share disposals meeting the detailed criteria.

A corporate shareholder not qualifying for the exemption described above may defer all or part of its tax liability on the sale of shares by accepting shares or loan notes issued by the purchasing company and holding over its chargeable gain until a further sale or repayment.

With effect from 1 April 2002 the UK introduced tax relief in relation to intellectual property held by a company which broadly provides that tax relief will be given according to the amortisation provided for in the accounts providing that this is in accordance with generally accepted accounting principles. This relief also extends to relief for amortisation charged in the accounts in respect of purchased goodwill.

The UK also has special tax relief provisions to assist companies engaged in Research and Development (R&D) which allow qualifying expenditure on R&D to be increased for tax deductibility purposes to either 150% or 125% of the expenditure incurred, depending on the qualifying status of the company.

5. Tying in or removing employees

A purchaser is often concerned to ensure that, as part of the transaction process, key employees are retained and that they do not have the ability to harm the business going forward. The common methods for ensuring this are via the terms of the employment contract itself and via incentivisation schemes. Equally, any purchaser will need to understand the implications, of and possible liabilities associated with, removing defined employees.

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Keeping key personnel

There are various contractual provisions which may be negotiated in order to ensure employee retention and protection of the business including the following:

- *Restrictive covenants*

These are express terms within an employment contract which allow an employer to prevent competition from an ex-employee following the termination of employment by restricting such individual's right to engage in a competing business, to solicit former customers and to poach former colleagues.

Prima facie, restrictive covenants are void as being in restraint of trade and are only enforceable where the employer has a legitimate business interest to protect, for example, a trade secret or other information which, if disclosed, would be liable to cause real or significant harm to the employer's business. The restraint must be reasonable in scope, time and area and must be no wider than is necessary to protect the employer's business.

A restrictive covenant will be unenforceable if the employer has no interest to protect or if the clause is too widely drafted although in these circumstances it may be subject to the "blue pencil" test whereby that part of the clause which is too wide is severed leaving the remainder in force. Enforcement is by way of injunction or damages.

Wrongful dismissal of an employee can render an otherwise valid restrictive covenant unenforceable because the covenant will "fall away" in the event of the employer's breach.

- *Garden leave*

"Garden leave" is a term used by employers to send employees home on full pay and benefits during their notice period. The purpose of a garden leave clause is to prevent employees obtaining further confidential information about the current employer that might be of use to any new employer. Contact with customers and suppliers is usually banned as is the entry onto company premises. Most contracts of key employees include a garden leave clause.

The contract of employment will still exist during the period of garden leave, however, the employer will be under no obligation to provide the employee with work. Until the recent Court of Appeal decision in *Symbian v Christensen* (May 2000) it was thought the implied duty of fidelity and good faith also continued during the period of garden leave. However, in *Symbian* it was held that putting an employee on garden leave, even though in accordance with the contract,

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fundamentally and irretrievably undermined the employer/employee relationship. All that remains is the bare contract and all that can be enforced against the departing employee are the express terms of the contract.

Accordingly, the contract should include express terms restricting the employee from working for others during the period of garden leave.

- *Incentivisation Schemes*

Various incentivisation shares are used to induce employee loyalty and increase performance.

- *Share Option Schemes*

The most common form of employee incentivisation is the share option scheme.

Share options in the UK fall into two classes. Those options which are Revenue approved and receive beneficial tax treatment and those which are unapproved. In recent years the government has reduced the tax benefits available under the approved plans so that most companies now operate both forms of plans alongside each other.

One of the disadvantages of the unapproved share option arrangements is that a National Insurance tax charge is levied in addition to an Income Tax charge on the gain in value attributable to the option shares. This burden is principally a liability of the employer but recent changes to legislation allow employers to agree with their employees that they will be responsible for payment of the National Insurance charge. However, for this to be effective in law, written agreement needs to be made between the employees and the employer and recorded in the share option plan documentation and rules.

As in the US, options tend to lapse on leaving employment or on change of employer subject to transitional provisions enabling employees to exercise options where there has been a sale of the business.

- *Pensions*

Pension provision in the UK has historically been provided through company sponsored occupational schemes providing pension benefits by reference to the member's salary at retirement. These schemes are known as "final salary" or "defined benefit" schemes. During the last ten years as the schemes have become more expensive to operate, many employers in the UK have switched to group money purchase schemes (also known as defined contributions).

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The essential difference between these two schemes is that under the final salary arrangement the financial risk will lie with the employer whereas under the money purchase scheme the financial risk will lie with the employee. This is because the investment fund allocated to each individual is utilised to purchase whatever annuity can be purchased in the market at the date of that individual's retirement. It is therefore the employee who bears the investment and market risks such that he or she will not know the amount of the pension until they actually retire. Increasingly, UK pension provision has been moving from group money purchase arrangements to group personal pensions. These are essentially individual contracts to which the employer contributes. Group personal pensions are becoming increasingly attractive to employers because they are far less regulated than occupational schemes.

All employers employing five or more employees who do not have an existing occupational scheme or an exempt personal pension have to designate a "Stakeholder" pension. This has been introduced by the UK government to ensure that lower paid employees have the opportunity to build up a low cost pension plan for themselves.

Scheme funding issues will be particularly relevant on a company acquisition. Pension rights do not, however, transfer under TUPE on a transfer of a business. This rule has been subject to some litigation in the UK and is now also subject to a consultation paper between industry and the government. It is possible that the general rule providing that pensions do not transfer as part of a business sale will change in the future. The current position has recently been clouded by a European court case holding that pension rights payable on a redundancy may transfer under TUPE.

Termination of Employment

In addition to the issues listed above relating to retention of employees, care must be taken if it is decided that certain staff are no longer required following the acquisition of the business or company.

If the purchaser aims to remove a director who is not an employee, it will be necessary to consider such director's services agreement to establish the basis upon which the agreement can be terminated. The individual will also need to resign his or her directorships and send the appropriate notifications to Companies House.

If the director is also an employee, care must be exercised when terminating the engagement because both contractual and statutory claims can arise. Careful consideration of the contract

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will ensure that no contractual terms are breached and that the appropriate notice is given and benefits maintained.

It will also be important to understand the implications of the statutory rights of employees which arise from length of employment. For example, the right not to be unfairly dismissed which arises when an employee has continuous employment. Care must be exercised when terminating the employment of an individual who satisfies the qualifying period. Employment can only be terminated fairly in specified circumstances, for example, on grounds of conduct and capability. The maximum compensatory award for unfair dismissal is £50,000, however, in addition, a basic award calculated with reference to salary and length of employment can be given.

It is important to note that there is no qualifying period necessary in order to bring a sex, race or disability discrimination claim. Moreover, an individual need not be an employee to pursue a discrimination claim. Such claims may be pursued by job applicants who feel they have not been successful at interview because of their sex, race or disability. There is no limit to the amount which can be awarded for compensation a successful discrimination claims.

The above material is designed to provide a summary of aspects of the subject matter covered. It does not purport to be comprehensive or render legal advice. The information is general in nature and should not be relied upon without seeking further advice. The material does not purport to cover matters relating specifically to the laws in Scotland or Northern Ireland. The law is stated at August 2002.

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MERGERS & ACQUISITIONS

Should we stay or should we go?

As the European Union prepares to open its doors to new members, **Michelle Thomas and Zanna Woods-Scawen of Eversheds** consider what impact will this have on companies seeking competitive advantage through low cost operations in Eastern Europe?

On 1 May 2004, ten more countries will join the European Union. Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia and Slovenia will each sign up to approximately 100,000 pages of European Union legislation, court decisions and policy commitments (known as the "acquis communautaire") with Bulgaria and Romania to follow in 2007.

The trend for moving certain business services and product areas, whether by way of outsourcing arrangement or simple internal transfer, particularly in the IT and telecommunications sectors, continues to grow as companies seek to take advantage of lower costs of production. What impact then is the forthcoming enlargement programme likely to have on business location and migration in Europe?

Business migration is by no means a new phenomenon, having been exploited for years by companies in the manufacturing sector who have understandably been attracted by the cost advantage that certain countries have to offer. These same companies may, however, soon find themselves in the position whereby they have a presence in countries which, although previously considered to be comparatively more cost effective with a close proximity to the relevant "gateways" of Western Europe, are themselves now on the threshold of full European Union membership.

The advantages for those countries acceding to the European Union are well rehearsed but what about those businesses currently located in these countries whose main aim in choosing the same was the decreased regulation and cost they assured in comparison to their European Union neighbours? This article aims to explore some of the legal issues which companies based in the new European Union accession countries will face from next year and consider the impact such changes will have on the decision companies must make on whether to stay or relocate to a jurisdiction outside of the European Union.

A time for legislative change

From day one, upon a new member state joining the European Union, it will be required to adopt the acquis communautaire, which will include all relevant European Union law. This comprises not only primary legislation, such as the EU Treaty which will have direct effect in the member states (ie it will automatically apply), but also secondary legislation, such as directives which must be incorporated into the national laws of each country. In addition, previous decisions of the European Court of Justice will have effect. The new member states will sign to an already well established and vast legal and regulatory framework.

Moreover, and for the most part, there will be no transitional phase in respect of the implementation. The new accession countries are well acquainted with the mammoth task ahead of them in adopting the entirety of European Union law as it exists on 1 May 2004. For this reason, many of them have already begun to introduce amendments to their national laws to ensure that they will be capable of complying with what is required of them. Some of these amendments have already taken effect, whilst some will not come into force until the date of accession.

But what does this mean for businesses located in these countries? In broad summary, it means compliance and this means adopting new procedures and systems. In short, it means changing the manner in which their existing business is conducted. Here are some examples:

The Work Force

Whilst European Union employment law has not been codified and all member states remain free to adopt their own national laws, such laws must conform to

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the European Union norms and requirements.

Companies based in the new accession states will need to amend their working practices to take account of a more regulated employer/employee relationship. Some of the major areas to note are:-

- Equal pay for men and women;
- Equal treatment based on gender and race;
- Right to parental leave;
- Acquired rights. This covers the situation where an undertaking, business or part of a business is transferred and gives employees certain rights to transfer with the business;
- Establishment of European works councils;
- Protection of employees in the event of the employer's insolvency;
- Health and safety in the workplace;
- Requirement to provide certain terms of employment in writing;
- Limitations on working time; and
- Right to minimum wages regardless of the industry, sector or the size of the employer's business.

And there will be a price tag to implementing an entirely new set of working practices and policies in order to comply. Some of the new European Union accession countries have already begun to put the framework in place through a combination of new laws and amendments to existing labour codes. Poland, for example, has made amendments to its Labour Code of 1974 which came into force recently on 1 July 2003.

Environmental

As with other areas, the new European Union member states must incorporate European Union environmental law into their national laws through the acquis communautaire. Not surprisingly, there are many regulations and directives covering environmental issues. Manufacturing companies and those involved in heavy industry in particular will feel the impact of implementing policies and practices to deal with, amongst others:-

- Industrial waste and waste storage;
- Transportation and disposal;
- Polluted water;
- Causes of air pollution;
- Radioactive and nuclear substances;
- Industrial emissions;
- Landfills;
- Labelling of dangerous substances;
- Impact and risk assessments; and
- Protection of plants and wildlife.

Anti-competitive Practices

Freedom of competition and the regulation of the same is an area which has the potential to have a significant impact on companies based in the new accession countries. The principles preventing anti-competitive actions are contained in Articles 81 to 87 of the EU Treaty and will therefore be of direct relevance to all businesses in the new member states.

More specifically, any restrictive agreement or related practice which has the potential to affect trade between European Union member countries will be automatically void. There are provisions which allow for individual exemptions and certain types of agreement can take the benefit of a block exemption provided the relevant terms comply with those permitted by the European Commission. Companies will also have to consider their market position as European Union competition law prevents any abuse of a dominant market position and the prices at which they sell into the European Union because of the anti-dumping provisions prohibiting exports to the European Union from non European Union countries at prices lower than those of the local market.

Companies doing business within the European Union must now take the time to check their trading arrangements to ensure that they do not fall foul of any of the European Union competition law provisions or decisions. Certain of the new accession states, such as Czech Republic and Lithuania, have already introduced legislation and block exemptions to meet the requirements of the EU Treaty.

Product Liability

Companies which fall within the remit of European Union legislation need to be aware of the various provisions governing product liability. For example, companies are under an obligation to submit to a general safety requirement for placing products on the market and must notify to national authorities any information which they possess in relation to unsafe products (although this can lead to costly compulsory product recalls). European Union law has also introduced a strict liability regime in relation to defective or unsafe products, which means that manufacturers need to be certain that their products are safe in order to avoid liability.

Taxation

The national laws of new member states will be required to comply with European Union law, such as the Merger Directive and the Parent-Subsidiary Directive.

In addition, from the first day of accession, new member states will join the European Single Market and the border of the European Union will widen. Companies based in the new accession countries who have previously paid import taxes to transport goods into the Union will no longer do so. Instead, the European Union Value Added Tax system will apply for sales and purchases within the Single Market. Conversely, the previous borders at which export duties from the European Union were payable will be extended to the borders of the new member states.

Accordingly, companies in the new accession countries will have to change their sales and purchase policies in limiting where they have previously traded with existing European Union member states in order to comply with the new regime to which they will belong which will in turn require the filing of many new tax returns as a result.

The wider impact – should we stay or should we go?

Clearly, there are many advantages of accession for those member states about to join the European Union. The legal compliance examples given above, whilst highlighting some of the key concerns for many companies, only skim the surface of the new regimes to which these countries will be subject. Accordingly, those businesses who conduct their activities in these countries will have a decision to make – to stay or go.

And the decision process will not solely comprise an analysis of hard cost. As barriers fall, entry to the European Union will allow free movement of goods and services, capital and labour (although the current member states will retain some control over the inflow of labour for up to seven years following enlargement).

Companies will see an increase in trade

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MERGERS & ACQUISITIONS

and competition throughout the enlarged Union, more common industrial and product standards and customs borders will be removed. In addition to these direct benefits, pan-European companies with bases in the new member states will be able to take advantage of a larger Union by arranging their operations and activities on a European wide basis rather than having to consider different parts of the business independently.

The new member states of the European Union will be hoping that companies will now consider them as progressive nations in which to invest. Indeed, some of the countries such as Poland, Hungary and Czech Republic have already made much progress in this area, with large foreign investments injected into sectors such as banks and utilities. Indeed, the kudos of becoming a member state of the European Union will do much to encourage further direct investment into these countries.

However, despite all the advantages that membership will bring, it cannot be ignored that many companies based in the new accession countries initially chose them as suitable business locations for well defined reasons, primarily the opportunity to establish and conduct business in close proximity with the existing European Union whilst, at the same time, enjoying a low cost base and competitive advantage. Legal compliance is only one factor in the total cost analysis but, as companies will be aware, it too has a price tag.

Indeed, whilst prices in the new accession countries remain lower than the average of prices within the existing fifteen member states of the European Union, following a report published by the European Commission in May 2003, it is widely expected that wages and prices generally will converge closer to European Union levels and indeed this has already started to occur in some of the new member states.

And if business does decide to migrate, what are the alternatives? It is almost certain that companies will at least consider relocating to less developed countries outside the European Union capable of offering an untapped resource of a competitive cost base. If this shift occurs, it is likely to be further eastwards to countries such as Bulgaria and Romania (although both are due to join the Union in 2007) or even Serbia, Croatia and other parts of former Yugoslavia. However, such moves are not without their drawbacks. Many countries are in the process of recovering from periods of political unrest or war and the lack of a refined infrastructure and necessary resources. For many companies, it will be a balancing act to find the right solution. It will certainly be interesting to see who stays and who goes following 1 May next year.

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