The Market for Corporate Control: New Insights from the Financial Crisis in Ireland

Blanaid Clarke[*]

I. INTRODUCTION

This Article offers an Irish perspective on the market for corporate control (MCC), which plays a fundamental role in corporate governance theory. The MCC was first proposed by Henry Manne in a short article in the *Journal of Political Economy* in 1965.[1] He argued that inefficient management[2] in listed companies is reflected in decreases in share prices as discontented shareholders sell their shares rather than replace management.[3] An opportunity thus arises for third parties to acquire these companies cheaply, replace the inefficient managers, and turn the companies around. As a result, "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."[4] The emphasis of the article—entitled *Mergers and the Market for Corporate Control*—was on the antitrust implications of the MCC.[5] But Manne noted that "the analysis . . . has important implications for a variety of economic questions[,]" particularly those relating to the separation of ownership and control in large corporations.[6] Manne argued that while one motivation for a merger might be the diminution of

---

[*] McCann FitzGerald Professor of Corporate Law, Trinity College Dublin. The author gratefully acknowledges Charles O'Kelley, Marc Moore, and the participants at the 2012 Berle IV Symposium in London for their valuable insights and comments.

1. *See* Henry G. Manne, *Mergers and the Market for Corporate Control*, 73 J. POL. ECON. 110 (1965).

2. Manne never completely dealt with the question of what constitutes "efficient management" in the article, although he did note, when considering the benefits of the MCC and its contribution to efficiency, that "apart from the stock market, we have no objective standard of managerial efficiency." *Id.* at 113.

3. *Id.* at 112.

4. *Id.* at 113.

5. *See* George J. Stigler, *Mergers and Preventive Antitrust Policy*, 104 U. PA. L. REV. 176 (1955). Manne refers to this article, which examines mergers through a competition lens emphasizing the economic cost of decreased competition.

6. Manne, *supra* note 1, at 112.

competition—a goal that involves social costs—a more likely motivation is the desire to improve corporate management.[7] Manne thus claimed that "the potential return from the successful takeover and revitalization of a poorly run company can be enormous."[8]

A consequence of this potential value, Manne explained, is that the MCC acts as an important constraint on management behavior in circumstances where the owners, as Berle and Means suggested,[9] lack appreciable control. He claimed that "only the take-over scheme provides some assurance of competitive efficiency among corporate managers and thereby affords strong protection to the interests of vast numbers of small, non-controlling shareholders."[10] It also affords shareholders "strong power,"[11] which, it has been noted, stands in marked contrast to the prevailing characterization, at the time Manne was writing, of shareholders as "chumps . . . routinely, and so predictably, bamboozled by managers supposedly advancing shareholder welfare but really maximising their own welfare."[12] Although Manne referred in the article to the replacement of inefficient managers, it is also clear that the MCC may exert a disciplinary effect by encouraging managers to improve their performance in order to avoid a takeover and the subsequent loss of employment.

Like much of Manne's work, *Mergers and the Market for Corporate Control* has been described quite correctly as "ground-breaking,"[13] "revolutionary,"[14] and "pioneering."[15] Roberta Romano argued that the article marked "the intellectual origin of what would become the new paradigm for corporate law."[16] She noted how Manne's contribution achieved recognition following advances in modern finance,[17] new research methodologies,[18] the economic theories of the firm,[19] and the ad-

7. *Id.* at 113.

8. *Id.*

9. ADOLF A. BERLE & GARDINER C. MEANS, THE MODERN CORPORATION & PRIVATE PROPERTY 69 (1932).

10. Manne, *supra* note 1, at 113.

11. *Id*. at 112.

12. Fred S. McChesney, *Manne, Mergers and the Market for Corporate Control*, 50 CASE W. RES. L. REV. 245, 249 (1999).

13. Daniel Fischel, *Efficient Capital Market Theory, the Market for Corporate Control, and the Regulation of Cash Tender Offers*, 57 TEX. L. REV. 1, 5 (1978).

14. McChesney, *supra* note 12, at 246.

15. Roberta Romano, *After the Revolution in Corporate Law*, 55 J. LEGAL EDUC. 342, 343 (2005).

16. *Id.*; *see also* William J. Carney, *The Legacy of "The Market for Corporate Control" and the Origins of the Theory of the Firm*, 50 CASE W. RES. L. REV. 215 (1999).

17. Romano, *supra* note 15, at 344–45.

18. *Id.* at 346.

19. *Id.* at 347.

vent of the hostile takeover era.[20] In 1984, John Coffee wrote, "[T]he claim that hostile takeovers generate a disciplinary force that constrains managerial behavior cannot seriously be disputed."[21] From the 1980s onward, the MCC was adopted by corporate law scholars examining how the legal system should respond to those developments and challenges.[22] Manne's contribution continues to stimulate and influence new generations of scholars; *Mergers and the Market for Corporate Control* is currently ranked as the twenty-ninth most cited law review article of all time, and it remains the most cited corporate law article.[23]

An acceptance of the value of the MCC has led many scholars to advocate managerial passivity in the face of premium tender offers. Frank Easterbrook and Daniel Fischel, in their seminal 1981 article *The Proper Role of a Target's Management in Responding to a Tender Offer,* noted that "[t]he tender bidding process polices managers whether or not a tender offer occurs, and disciplines or replaces them if they stray too far from the service of the shareholders."[24] Describing this as "the most powerful check on agency costs," they concluded that the prevailing legal rules allowing the target's management to engage in defensive tactics in response to a tender offer decreases shareholders' welfare.[25] Although the U.S. courts did not adopt such a restrictive approach, Romano suggested that this literature constituted "one of many factors affecting courts' perception of takeovers, and, in particular, the Delaware Supreme Court's 1985 revision of the fiduciary standard applicable in the hostile takeover context."[26] *Mergers and the Market for Corporate Control* has also had a profound effect on public policy both in the United States and beyond. As discussed further below, it formed part of the rationale put forward in support of regulation promoting an unconstrained and active takeover market in the European Union at a national and supranational level.

In an ever-changing legal and economic environment, it is incumbent on us to subject all such premises to scrutiny in order to consider their continued application. This Article considers the effect of the MCC on the management of Irish credit institutions in the run-up to the finan-

20. *Id.* at 347–48.

21. John C. Coffee, Jr., *Regulating the Market for Corporate Control: A Critical Assessment of the Tender Offer's Role in Corporate Governance*, 84 COLUM. L. REV. 1145, 1294 (1984).

22. Romano, *supra* note 15, at 343.

23. Fred R. Shapiro & Michelle Pearse, *The Most-Cited Law Review Articles of All Time*, 110 MICH. L. REV. 1483, 1490 (2012).

24. Frank H. Easterbrook & Daniel R. Fischel, *The Proper Role of a Target's Management in Responding to a Tender Offer*, 94 HARV. L. REV. 1161, 1169 (1981).

25. *Id*. at 1196.

26. Romano, *supra* note 15, at 349.

cial crisis. Part II sets the background by explaining how the MCC has become an integral part of takeover regulation in Europe. The weaknesses in the efficient market hypothesis, which underlie the MCC and are summarized in Part III, appear not to have undermined the theory's credibility in the minds of public policy makers in Europe. Part IV explains the background of the financial crisis in Ireland, and Part V considers the effect of the MCC on management of Irish credit institutions in the run-up to this crisis. A number of reports on the causes of the crisis in Ireland have identified corporate governance failures and, in particular, poor risk management and inappropriate remuneration structures in the years leading up to the crisis. These findings are consistent with similar studies of the financial crisis commissioned in other jurisdictions across the world. A concern is that this mismanagement does not appear to have been reflected in reduced share prices as the MCC would have predicted. In fact, the opposite occurred—share prices in credit institutions soared.[27] This Article argues not only that the MCC did not have the anticipated disciplinary effect on management, but also that it may have had the opposite effect. It appears as if certain boards may have acted recklessly in order to maintain share prices to stave off takeover bids.

II. DIRECTIVE 2004/25/EC ON TAKEOVER BIDS

The impact of the MCC theory on European takeover policy may have been even more profound than its influence in the United States. This may be explained in part by the significant influence exerted on European takeover regulation by the U.K. Panel on Takeovers and Mergers (U.K. Panel) through its City Code on Takeovers and Mergers (the Code). Historically, the U.K. market for takeovers constituted over 50% of the whole E.U. market for corporate control,[28] and the U.K. Panel, established in 1968, possesses unrivalled experience of takeovers and acknowledged expertise in the field of takeover regulation.[29] In 1974, the European Commission (Commission) invited Professor Pennington, a U.K. company law expert, to produce a proposal for a draft directive on

27. *See* RANU DAYAL ET AL., LIVING WITH NEW REALITIES: CREATING NEW VALUE IN BANKING 2009 (2009), *available at* http://www.bcg.com/documents/file15429.pdf. The share prices of financial institutions worldwide did not begin to decline until mid-2007 and the decline then became most dramatic in the third quarter of 2008.

28. MARCCUS PARTNERS, THE TAKEOVER BIDS DIRECTIVE ASSESSMENT REPORT 285 (2012), *available at* http://ec.europa.eu/internal_market/company/docs/takeoverbids/study/study_en.pdf (noting that since the financial crisis, the number of takeovers in the United Kingdom has declined whilst the number in continental Europe has remained relatively stable).

29. *See* Andrew Johnston, *Takeover Regulation: Historical and Theoretical Perspectives on the City Code*, 66 CAMBRIDGE L.J. 422 (2007).

takeovers.[30] Many of the proposal's features are modeled on the Code. One of these is the board-neutrality rule, which is reflected in the Code's general principle that shareholders should not be denied an opportunity to decide on the merits of a takeover,[31] and the rule that boards of offeree companies are prohibited from defending a bid unless shareholder approval is granted.[32] Although offeree company boards may mount a robust defense[33] or seek a white knight,[34] they are not permitted to unilaterally frustrate a bid.[35]

The Commission published the first draft directive in 1989,[36] but agreement on the substance and even the form of this legislation proved extremely difficult due to the significant differences between member states' capital markets, corporate governance regimes, and political cultures.[37] Following intense negotiations at the European Council Working Group[38] and at the Commission,[39] the Commission in 2001 compiled and submitted a directive to the European Parliament.[40] This proposal contained a board-neutrality rule that would have restricted defensive actions performed by the board without the prior authorization from the shareholders.[41] The restriction would have applied at least from the time the board became aware of the decision to make an offer or, if member states

30. *See* ROBERT R. PENNINGTON, REPORT ON TAKEOVERS AND OTHER BIDS (1974).

31. General Principle 3 states, "The Code is designed principally to ensure that shareholders in an offeree company are treated fairly and are not denied an opportunity to decide on the merits of a takeover and that shareholders in the offeree company of the same class are afforded equivalent treatment by an offeror." PANEL ON TAKEOVERS AND MERGERS, THE CITY CODE ON TAKEOVERS AND MERGERS, gen. princ. 3 (10th ed. 2011).

32. *Id.* r. 21.

33. The defense would be subject, of course, to compliance with the City Code including, for example, rule 19, which imposes a high standard of care and regulates documents, advertisements, interviews, debates, and other materials and interactions.

34. This is subject to rule 20.2, which ensures a degree of equality of information for competing offerors.

35. Simon Deakin & Ajit Singh, *The Stock Market, the Market for Corporate Control and the Theory of the Firm: Legal and Economic Perspectives and Implications for Public Policy*, *in* THE MODERN FIRM, CORPORATE GOVERNANCE AND INVESTMENTS 12–13 (Bjuggren, P. O. & Mueller, D. eds., 2008), *available at* http://www.cbr.cam.ac.uk/pdf/WP365.pdf (noting that related aspects of company and securities law in the United Kingdom, such as statutory preemption rights and the proper-purpose rule, also prevent certain potentially defensive behaviors by corporate boards).

36. Proposal for a Thirteenth Council Directive on Company Law Concerning Takeover and Other General Bids, 1989 O.J. (C 64) 8.

37. *Communication from the Commission to the Council and the European Parliament - Modernising Company Law and Enhancing Corporate Governance in the European Union - A Plan to Move Forward*, para. 3.1, COM (2003) 284 final (May 21, 2003).

38. The European Council Working Groups function as preparatory bodies for the Council of Ministers and are comprised of national officials with expertise in the areas under discussion.

39. *See* 1996 O.J. (C 162) 5; *see also* 1997 O.J. (C 378) 10.

40. 2001 O.J. (C 23) 1.

41. *Id.* art. 9(1).

required, as soon as the board became aware that an offer was imminent. A tied vote ensued and the proposed directive was accordingly rejected with the proposed board-neutrality rule receiving particular criticism.[42] Parliamentarians appeared to be particularly concerned that this rule would create an uneven playing field between the European Union and the United States. The discrepancy would be on the basis of the broad discretion afforded to the boards of American companies to utilize defensive devices pursuant to the business judgment rule, and also the stakeholder statutes that apply in many individual states.[43]

The Commission subsequently appointed a high-level group of company law experts to consider the matters raised by Parliament.[44] This group opined that in the light of available economic evidence, the availability of a mechanism to facilitate takeover bids would be beneficial.[45] It cited three reasons for this: the exploitation of synergies, the opportunity to sell at a premium on market price, and the market for corporate control.[46] In relation to the latter point, the group noted that "actual and potential takeover bids are an important means to discipline the management of listed companies with dispersed ownership . . . . Such discipline of management . . . is in the long term in the best interests of all stakeholders, and society at large."[47] Thus, the group concluded that "any regime which confers discretion on a board to impede or facilitate a bid inevitably involves unacceptable cost and risk."[48] This acknowledgement marks a resounding acceptance of the MCC. In response to the concern that European companies would be detrimentally affected by the disparity of treatment of companies in the United States referred to above, the group determined that the American approach was less likely to benefit the development of efficient, integrated capital markets in Europe because the legal and capital market environment is significantly differ-

---

42. *See* JAAP WINTER ET AL., REPORT OF THE HIGH LEVEL GROUP OF COMPANY LAW EXPERTS ON ISSUES RELATED TO TAKEOVER BIDS (2002), *available at* http://ec.europa.eu/internal_market/company/docs/takeoverbids/2002-01-hlg-report_en.pdf; *see also* Blanaid Clarke, *The Takeovers Directive: Is a Little Regulation Better Than No Regulation?* 15 EUR. L.J. 174 (2009) (noting Parliament also argued that the protection for employees of companies involved in the bid was insufficient).

43. WINTER, *supra* note 42, at 39–42.

44. Press Release, Company Law: Commission Creates High Level Group of Experts (Apr. 9, 2001), *available at* http://europa.eu/rapid/pressReleasesAction.do?reference=IP/01/1237&format=HTML&aged=1&language=en&guiLanguage=en.

45. WINTER, *supra* note 42, at 19.

46. *Id.*

47. *Id.*

48. *Id.* at 21.

ent.[49] It specifically referred to the existence of greater pressure to enhance shareholder value on American boards from nonexecutive directors, investment banks and institutional investors, heightened media scrutiny, proxy contests, and a larger number of liability suits against directors because derivative actions are easier to bring and the judicial system is better equipped to handle these issues.[50] The group also noted that antitakeover rules are controversial even within the United States, and that while some accept them as the outcome of regulatory competition among the states and effective lobbying by the business community, there is a large body of both economic and legal literature arguing that such rules should be prohibited.[51]

In 2004, Directive 2004/25/EC on Takeover Bids (the Directive) was finally passed.[52] Although the board-neutrality rule was left in the Directive, a compromise proposal by the Portuguese Presidency was included, thereby rendering the provision optional for member states[53] and also allowing member states to adopt a reciprocity rule.[54] Nineteen of the twenty-seven member states adopted the board-neutrality rule, although its effect is somewhat diminished by the fact that five of these states opted to make reciprocity available.[55] In its recent review of the Directive, the Commission reported that the board-neutrality rule has been a "relative success"[56] in terms of its implementation, and the Commission is not proposing to make the rule mandatory.[57] In coming to this conclusion, the Commission relied on an assessment report on the Directive indicating that stakeholders found that the optional board-neutrality rule had

49. *Id.* at 40–42. The Group also noted that European companies have benefited from the intensive takeover activity in the United States, and that a number of defensive tactics are introduced to protect shareholders from partial bids, which are not allowed in the Directive.

50. *Id.* at 41.

51. *Id.* at 42.

52. Council Directive 2004/25, 2004 O.J. (L 142) 12 (EC).

53. *Id.* art. 12.1. Member states may opt out of adopting the board-neutrality rule under article 9, but in such a case article 12.2 provides that they must allow individual companies to voluntarily apply the rule. A similar compromise applies to the breakthrough rule applied in article 11 of the Directive.

54. *Id.* art. 12.3. Member states may exempt companies that choose to opt in to the board-neutrality rule or the breakthrough rule to not apply the rule if they become the subject of a bid from an offeror who has not applied the same rule.

55. Paul L. Davies, Edmund-Philipp Schuster & Emilie Van de Walle de Ghelcke, *The Takeover Directive as a Protectionist Tool?* 14 (Eur. Corporate Governance Inst., Working Paper No. 141/2010, 2010), *available at* http://ssrn.com/abstract=1554616.

56. *Report from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions: Application of Directive 2004/25/EC on Takeover Bids*, at 8, COM (2012) 347 final (June 28, 2012), *available at* http://ec.europa.eu/internal_market/company/docs/takeoverbids/COM2012_347_en.pdf.

57. *Id.* at 10.

contributed to the openness of the European Union's MCC,[58] but that there was "little appetite to change."[59] The report endorsed the MCC theory by accepting that "transfers of corporate control (takeovers) may result in a more efficient allocation of control if the offeror presents a higher valuation of control because it is capable of using the pool of assets in the offeree company to generate greater value than the incumbent."[60] But the report concluded that the board-neutrality rule had only a moderate economic impact: although it may have increased the incentives to make an offer by removing post-bid defenses, it may also have reduced the potential premium paid by the offeror and encouraged incumbent shareholders to entrench before an offer is made.[61]

III. THE EFFICIENT MARKET HYPOTHESIS

In finance, capital market efficiency is the notion that all available information about a company is fully reflected in share price.[62] The view generally put forward is that markets are "semi-strong" in the sense that prices adjust rapidly in response to fluctuations in public information.[63] In *Mergers and the Market for Corporate Control,* Manne accepted that "a fundamental premise" underlying the market for corporate control is "the existence of a high positive correlation between corporate managerial efficiency and the market price of shares of that company."[64] He noted that there are "compelling reasons"[65] for believing that this correlation exists. He explained in a footnote:

> Insiders, those who have the most reliable information about corporate affairs, are strongly motivated financially to perform a kind of arbitrage function for their company's stock. That is, given their sense of what constitutes efficient management, they will cause share prices to rise or decline in accordance with that standard.[66]

---

58. MARCCUS PARTNERS, *supra* note 28, at 209.

59. *Id*. at 355.

60. *Id*. at 320.

61. *Id*. at 357.

62. Eugene Fama, *Efficient Capital Markets: A Review of Theory and Empirical Work*, 25 J. FIN. 383, 383 (1970).

63. Ronald J. Gilson & Reinier Kraakmann, *The Mechanisms of Market Efficiency* 70 VA. L. REV. 549, 644 (1984).

64. Manne, *supra* note 1, at 112.

65. *Id.*

66. *Id.* Manne used the term "insiders" to refer to persons presently controlling the affairs of the company. One way in which Manne suggested that insiders push share prices in the right direction is by insider dealing. *See* HENRY G. MANNE, INSIDER TRADING AND THE STOCK MARKET (1966). He also acknowledged the role of explicit public disclosure of information, sanctioned communication of information to financial analysts, and "derivative" trading, which occurs after some

Manne continued by explaining that dealings by shareholders, or potential shareholders, operating without reliable information will be "randomly distributed,"[67] yielding a neutral effect. On the other hand, dealing by insiders will move the average market price of a company's shares to the "correct"[68] one because they are not random.

In 2003, Lynn Stout noted that it was not necessary to have waited several decades to develop the suspicion that "efficient market theory fails, in some fundamental respect, to capture the reality of securities markets."[69] Nor, she states, "need we have suffered through the [c]rash of 1987 and the 1990s tech stock bubble to find enlightenment."[70] Stout argues that the weaknesses of the efficient market theory were apparent to anyone who cared to look for them. Within a few years after the theory was first developed and disseminated, "the trickle of legal articles questioning the market's efficiency had become a flood."[71]

In the aftermath of the banking crisis in the United Kingdom, the Chancellor of the Exchequer asked Lord Turner, the Financial Services Authority Chairman, to review and make recommendations for reforming U.K. and international approaches to banking regulations.[72] The resulting report published in March 2009 stated that the assumptions underlying the efficient market theory have been subject to increasingly effective criticism, "drawing on both theoretical and empirical arguments."[73] Behavioral economic theories suggest that the markets are vulnerable to socio-psychological factors such as herding, noise, and bubbles.[74] As noted by Lord Turner, "[m]any market participants accept on the basis of pragmatic observation that significant temporary bubbles in market prices are possible."[75] Lord Turner concluded that there is also evidence of pervasive and systemic biases in the marketplace,[76] and that

form of "market signalling." *See* Henry G. Manne, *Insider Trading: Hayek, Virtual Markets, and the Dog That Did Not Bark*, 31 J. CORP. L. 167 (2005).

67. *Id*.

68. *Id*.

69. Lynn A. Stout, *The Mechanisms of Market Inefficiency*, 28 J. CORP. L. 635, 637 (2003).

70. *Id.*

71. *Id.* at 667; *see also* Nicholas Wolfson, *Efficient Markets, Hubris, Chaos, Legal Scholarship and Takeovers*, 63 ST. JOHN'S L. REV. 511 (1989); Lynn A. Stout, *On the Nature of Corporations*, U. ILL. L. REV. 253 (2005).

72. FIN. SERVS. AUTH., THE TURNER REVIEW: A REGULATORY RESPONSE TO THE GLOBAL BANKING CRISIS (2009), *available at* http://www.fsa.gov.uk/pubs/other/turner_review.pdf.

73. *Id.* at 40.

74. *See* ROBERT J. SHILLER, IRRATIONAL EXUBERANCE (2d ed. 2005); Donald C. Langevoort, *The Behavioral Economics of Mergers and Acquisitions*, 12 TRANSACTIONS: TENN. J. BUS. L. 65 (2011).

75. FIN. SERVS. AUTH., *supra* note 72, at 40.

76. *See, e.g.*, DANIEL KAHNEMAN, PAUL SLOVIC & AMOS TVERSKY, JUDGMENT UNDER UNCERTAINTY: HEURISTICS AND BIASES (1982); Fischer Black, *Noise*, 41 J. FIN. 529 (1986); Ronald

policymakers have to recognize that "all liquid traded markets are capable of acting irrationally, and can be susceptible to self-reinforcing herd and momentum effects."[77]

A further weakness is evidenced by the inability of the efficient market hypothesis to accommodate derivatives trading. The hypothesis depends on an even flow of information through to the market, and experience has demonstrated that derivative trading can lead to information asymmetries and ultimately price inefficiencies in the marketplace. An example of such an asymmetry exists between informed contracts for difference holders and uninformed investors.[78] Manne's explanation of the MCC expressly assumes that insiders always have complete knowledge, whereas the advent of derivatives trading has changed that. Henry Hu recently argued that the twenty-first century financial system is simply becoming "too complex to depict."[79]

IV. THE IRISH BANKING EXPERIENCE

Ireland experienced one of the most catastrophic financial crises in the developed world.[80] In 2012, the cost to the taxpayers of bank recapitalization was estimated at approximately €64.1 billion ($80.4 billion)[81] with expectations that this figure may continue to rise. In addition, write-downs of shareholder funds in the banks covered by the government guarantee[82] and write-downs of shareholder funds at the foreign banks operating in Ireland were estimated at €29 billion ($36.4 billion) and €28 billion ($35.1 billion), respectively.[83] Liability-management exercises amounted to an additional €14 billion. To put those figures in context,

---

Gilson & Reinier Kraakmann, *The Mechanisms of Market Efficiency Twenty Years Later: The Hindsight Bias*, 28 J. CORP. L. 715 (2003); Andrei Shleifer & Lawrence Summers, *The Noise Trader Approach to Finance*, 4 J. ECON. PERSP. 19 (1990).

77. FIN. SERVS. AUTH., *supra* note 72, at 41.

78. For example, the holder of a long contract for difference position will be aware, based on market practice, that when the contract is closed out, there is likely to be ready access to the underlying securities. FIN. SERVS. AUTH., DISCLOSURE OF CONTRACTS FOR DIFFERENCE: FEEDBACK ON CP08/17 AND FINAL RULES 7 (2009).

79. *See* Henry Hu, *Too Complex to Depict? Innovation, "Pure Information" and the SEC Disclosure Paradigm*, 90 TEX. L. REV. 1601 (2012).

80. *See* Blanaid Clarke & Niamh Hardiman, *Crisis in the Irish Banking System* (UCD Geary Inst. Discussion Paper Series, Working Paper No. 2012/03, 2012), *available at* http://ssrn.com/abstract=2008302.

81. 772 DÁIL DEB. no. 1, at 86 (July 17, 2012), *available at* http://debates.oireachtas.ie/dail/2012/07/17/00086.asp.

82. *See* CREDIT INSTITUTIONS (ELIGIBLE LIABILITIES GUARANTEE) SCHEME 2009: DRAFT SCHEME FOR THE GUARANTEE BY THE MINISTER FOR FINANCE OF ELIGIBLE LIABILITIES SUBJECT TO THE APPROVAL OF THE OIREACHTAS (2009), http://www.finance.gov.ie/documents/publications/statutoryinstruments/2009/guaranttdraftsch09.pdf.

83. *See* Clarke & Hardiman, *supra* note 80.

Ireland's total gross domestic product in 2011 was €159 billion.[84] Nearly half of these losses are attributable to a single bank, Anglo Irish Bank,[85] with most of the remaining losses being incurred by Ireland's two oldest banks: the Bank of Ireland and Allied Irish Bank.[86] All three banks, together with Irish Life and Permanent, a former building society, were listed on the Irish and London Stock Exchanges. This means that theoretically they had broad shareholder bases and were thus exposed to the MCC.

In an effort to understand the causes of Ireland's banking crisis, three reports have been produced at the bequest of the Irish government. The first report was prepared by the Governor of the Central Bank, Patrick Honohan.[87] The second report was prepared by Klaus Regling, a German economist and current Chief Executive Officer of the European Financial Stability Facility, together with Max Watson, previously a senior adviser on economic and financial affairs at the European Commission and Deputy Director in the IMF.[88] The final report was prepared by Peter Nyberg, a Finnish economist and previous Director General of the Financial Markets Department in the Finnish Ministry of Finance.[89] While all three reports concluded that Ireland's crisis bears the clear imprint of global influences, the crisis was in crucial ways "home-made."[90] Unlike the United States or Britain, Ireland's enormous banking exposure did not stem from a proliferation of complex financial products or exposure to the United States subprime mortgage market. Instead, Ireland's banking crisis was described by Regling and Watson as "a plain vanilla property bubble, compounded by exceptional concentrations of lending for purposes related to property and notably commercial property."[91] So, while international pressures did contribute to the timing, intensity, and depth of the Irish banking crisis, the essential characteristic of the problem was domestic and classic.[92]

---

84. CENT. STATISTICS OFFICE, MEASURING IRELAND'S PROGRESS 17 (2012).

85. Anglo Irish Bank (along with the Irish Nationwide Building Society) is now re-titled Irish Bank Resolution Corporation Limited.

86. 772 DÁIL DEB., no. 1, at 86.

87. *See* PATRICK HONOHAN ET AL., THE IRISH BANKING CRISIS: REGULATORY AND FINANCIAL STABILITY POLICY (2010), *available at* http://mpra.ub.uni-muenchen.de/24896/1/MPRA_paper_24896.pdf.

88. *See* KLAUS REGLING & MAX WATSON, A PRELIMINARY REPORT ON THE SOURCES OF IRELAND'S BANKING CRISIS (2010), *available at* http://www.bankinginquiry.gov.ie/Preliminary%20Report%20into%20Ireland's%20Banking%20Crisis%2031%20May%202010.pdf.

89. *See* PETER NYBERG, COMMISSION OF INVESTIGATION INTO THE BANKING SECTOR IN IRELAND (2011), *available at* http://www.bankinginquiry.gov.ie/.

90. REGLING & WATSON, *supra* note 88, at 5; *see also* HONOHAN ET AL., *supra* note 87, at 134; NYBERG, *supra* note 89, at 96–99.

91. REGLING & WATSON, *supra* note 88, at 6.

92. HONOHAN ET AL., *supra* note 87, at 22.

A number of macroeconomic conditions played a role in triggering Ireland's banking crisis. Ireland's use of the euro brought access to cheap finance both for the banks and for their customers.[93] Demand for credit was particularly high amongst builders and property developers.[94] Competition between the Irish lending institutions, including the nondomestic banks, intensified. As they desperately sought to hold their share of the rapidly expanding market, new lending instruments such as tracker mortgages and 100% loans were offered, and the loan approval processes became more streamlined.[95] Anglo Irish Bank, for example, was proud of its reputation as "a relationship lender" and went to great lengths to accommodate its top clients.[96] Nyberg characterized the environment as one in which the supply of credit available exceeded demand for good-quality loans.[97] The three-fold increase in average real-property prices from 1994 to 2006 was described by Honohan as "the highest in any advanced economy in recent times,"[98] and one which, "long before it peaked, looked unsustainable to most commentators."[99] As Anglo's profits increased, and as it was rewarded by staggering growths in its share price, the larger and traditionally more conservative banks—Bank of Ireland and Allied Irish Bank—came under increasing pressure to relax their own loan-approval and risk-assessment practices in order to keep pace.[100]

A further contributing factor to the Irish crisis was the existence of significant corporate governance failures. Because of the small marketplace, significant groupthink and lack of diversity on the boards appear to have exacerbated the problem.[101] Regling and Watson identified four key areas in which poor bank management and governance contributed to the Irish banking crisis. First, management failed to appreciate the risk entailed by the significant concentration of bank assets in activities related to property, and especially non-household-based commercial property. Property-related lending grew by 29.4% and speculative commercial and property lending grew by an average of 56.5% each year between

93. REGLING & WATSON, *supra* note 88, at 12.

94. NYBERG, *supra* note 89, at 20.

95. *Id.* at 21. "Tracker mortgages" are mortgages whose rates vary in accordance with the European Central Bank base interest rate.

96. *Id.* at 32. This was driven not merely by a desire to demonstrate loyalty to old customers but also by the fear that such customers would find the finance from their banking competitors.

97. *Id.*

98. HONOHAN ET AL., *supra* note 87, at 24.

99. *Id.*; *see also* Patrick Honohan, *Resolving Ireland's Banking Crisis*, 40 ECON. & SOC. REV. 207 (2009).

100. NYBERG, *supra* note 89, at 34–35.

101. *Id*. at 86.

2002 and 2007.[102] Domestic-property lending represented 80% of all growth in credit.[103] Second, lending guidelines and processes appear to have been widely circumvented.[104] Third, poor remuneration policies that encouraged and rewarded risk-taking were tolerated. For instance, in 2007, the Chief Executive of Anglo Irish Bank, David Drumm, received total remuneration for the year of €3.3 million including a €2 million bonus.[105] Drumm's Bank of Ireland and Allied Irish Bank counterparts received €2.97 million and €2.1 million, respectively.[106] The Anglo Irish Bank Chairman, Sean Fitzpatrick, received fees of €431,000 that year, and the total package for the fourteen members of the board was €9.63 million.[107] The fourth failure involved "very specific and serious breaches of basic governance principles"[108] concerning identifiable transactions in specific institutions including undisclosed loans to directors, creative accounting, and loans to investors to purchase bank shares.[109] In considering the reaction of the market to these four failings, it is important to note that only the last one would not have been outwardly evident to the public.

V. THE OPERATION OF THE MCC IN THE IRISH BANKING SECTOR

Before examining the market's reactions to the aforementioned corporate governance failings, it is necessary to consider the nature of the market for corporate control in Ireland. Share ownership in Ireland is relatively widely dispersed, and the level of takeover activity is reasonably high.[110] As the table below demonstrates, since 1997, there has been an average of 5.3 takeovers per year from an annual average of seventy-five relevant companies. In that time, there have been only seven hostile takeover offers (an average of 0.5 per year), and none of these takeovers have been successful. In four of the bids, a preferred bidder ultimately acquired the targets, and in the remaining three bids, control did not pass and the targets remained independent. In two of the latter instances, competition issues may have caused a significant barrier to the acquisition.

---

102. *Id*. at 17.

103. *Id*. at 14.

104. *See id.* at 96–97; REGLING & WATSON, *supra* note 88, at 35.

105. ANGLO IRISH BANK, ANNUAL REPORTS & ACCOUNTS 126 (2007), *available at* http://www.ibrc.ie/About_us/Financial_information/Archived_reports/Annual_Report_2007.pdf.

106. *Id.*

107. *Id.*

108. REGLING & WATSON, *supra* note 88, at 35.

109. *Id.* at 35, 36.

110. MARCCUS PARTNERS, *supra* note 28, at 284 (noting a significant decrease in takeovers in Europe in the aftermath of the financial crisis, with the average value of deals in 2010 reduced to the level in 2003 and an even greater decrease in the number of deals).

Figure 1: Level of Takeover Activity in Ireland[111]

Year End	"Takeovers" Supervised (Number of Companies Involved)	Number of Hostile Bids	Number of Relevant Companies	Percentage of Companies subjected to a Bid
1998	5	0	78	6.4%
1999	7 (6)	1	80	7.5%
2000	8 (7)	1	77	9.1%
2001	8	0	79	10.1%
2002	7 (6)	1	76	7.9%
2003	9	0	67	13.4%
2004	4 (3)	0	64	4.7%
2005	2	0	66	3.0%
2006	3	0	82	3.6%
2007	8	1	83	9.6%
2008	9	0	81	11.1%
2009	1	1	79	1.2%
2010	8(7)	2	75	9.3%
2011	4 (3)	0	70	4.3%

The Irish Takeover Panel is the supervisory authority responsible for monitoring takeovers of relevant Irish companies. It took over this role from the London Panel, which monitored Irish companies until 1997.[112] The Takeover Rules of the 1997 Irish Takeover Panel Act, though in statutory form, are derived from the City Code and are very similar in substance. Rule 21 of the Irish Takeover Rules sets out a board-neutrality rule that, like its U.K. counterpart, requires shareholder approval for actions that might frustrate a takeover or deprive shareholders of the opportunity to consider a bid.[113] When implementing the Take-

111. The data in figure 1 was compiled from the Irish Takeover Panel's annual reports from 1997 to 2011, which are available at http://www.irishtakeoverpanel.ie/about/annual-reports/. "Relevant companies" primarily include Irish registered companies listed on the Irish Stock Exchange, the London Stock Exchange, the New York Stock Exchange, and Nasdaq. *See* Irish Takeover Panel Act 1997 § 2 (Act No. 5/1997) (as amended by § 75 of the Investment Funds, Companies and Miscellaneous Provisions Act in 2005 and § 26 of the Investment Funds, Companies and Miscellaneous Provisions Act in 2006), *available at* http://www.irishstatutebook.ie/pdf/1997/en.act.1997.0005.pdf. The term "takeover" is defined in the 1997 Irish Takeover Panel Act and includes schemes of arrangement.

112. Blanaid Clarke, *The Irish Takeover Panel Act, 1997: A Further Cutting of the UK Regulatory Ties*, *in* 1 PALMER'S COMPANY LAW 1 (Geoffrey Morse ed., 1998).

113. Takeover Rules 2007 r. 21, Irish Takeover Panel Act 1997.

overs Directive in 2006,[114] Ireland also maintained its position on neutrality and did not adopt the reciprocity rule. Thus, it can be said that Ireland, too, seeks to ensure an unconstrained takeover market. The Irish Panel, as required by the Directive, also applies a mandatory-bid rule.[115] This means that an acquisition of securities that leads to the acquirer, together with any concert party, holding 30% or more of securities conferring voting rights in the company triggers an obligation to make a bid for the entire share capital.[116]

Control structures and barriers to takeovers, such as pyramid structures and cross-shareholdings, are uncommon in Ireland and not covered by the Directive. National competition law would have been a factor in deterring the main Irish credit institutions from launching takeover bids for each other. E.U. merger controls could have been seen as a barrier to acquisitions from related institutions. Sectorial regulation may also have been a consideration, as prior notification to, and approval of, the Central Bank, and in certain cases the Minister for Finance, is required for proposals to acquire specific holdings in Irish banks.[117] A holding of 10% of the total shares or of the total voting rights attaching to shares would typically fall within the scope of this requirement,[118] although the Central Bank may exempt such a transaction if it is entered into with the Central Bank's prior approval "in the interests of the proper and orderly regulation of banking or financial markets in the State."[119] It is submitted that despite these regulatory restrictions, the Irish banks would still have been subject to the MCC.

Applying the MCC to the Irish credit-institution market suggests that the share prices of the listed institutions should have dropped to reflect their increasingly poor risk management and corporate governance, and consequently the institutions should have been acquired and improved. Yet, as figure 2 below demonstrates, this did not happen. Profits in the four banks, and Anglo Irish Bank in particular, grew significantly. Demand for shares grew, and from January 2000 to its peak in February 2007, the combined market capitalization of the four banks rose from €20.4 billion to €57.4 billion. In this period, Anglo's market capitalization grew over 2,000% from €0.6 billion in early 2000 to a peak of €13.3 billion in mid-2007.

114. Council Directive 2004/25, 2004 O.J. (L 142) 12 (EC).

115. *Id.* art. 5.

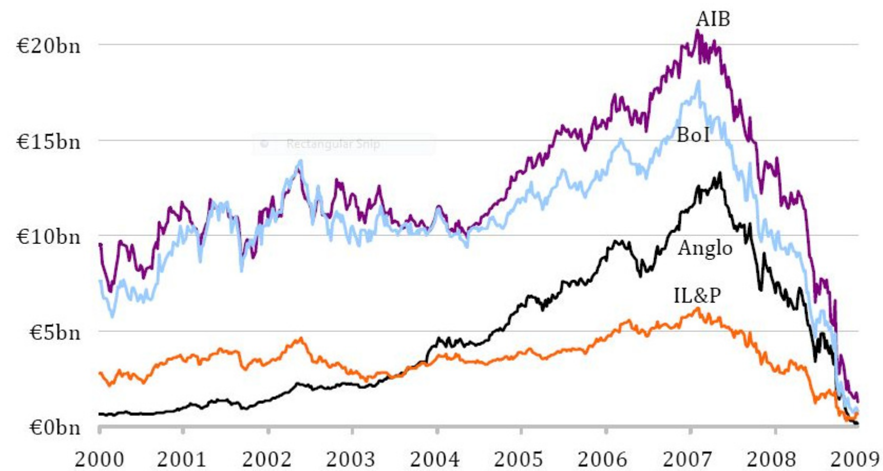
116. Irish Takeover Panel Act 1997 r. 9.

117. *See* The Central Bank Act 1989 (Act No. 16/1989) (Ir.), *available at* http://www.irishstatutebook.ie/1989/en/act/pub/0016/index.html.

118. *Id.* § 74.

119. *Id.* § 75(2).

Figure 2: Individual Market Capitalizations of Listed Covered Banks 2000–January 2009[120]



It seems clear from a study of these prices that shareholders did not desert the Irish banks in droves as Manne predicted. Instead, they increased their level of investment, thereby driving share prices upward. It was only when "the music"[121] stopped in mid-2007 that interbank lending slowed down and share prices began to decline due to market fears of overexposure to potential losses on high-risk U.S. mortgages. Then the Northern Bank run in September 2007,[122] its nationalization in February 2008,[123] followed by the failure of Fannie Mae and Freddie Mac in July 2008,[124] led market analysts and credit-rating agencies to express concern about the stability of the banks.[125] Lehman Brothers collapsed in September 2008,[126] and the share prices of credit institutions

120. NYBERG, *supra* note 89, at 14 (listing the Irish Stock Exchange as its source).

121. Michiyo Nakamoto & David Wighton, *Citigroup Chief Stays Bullish on Buy-outs*, FIN. TIMES (July 9, 2007), http://www.ft.com/intl/cms/s/0/80e2987a-2e50-11dc-821c-0000779fd2ac.html # axzz29PQ62D2S.

122. Press Release, Bank of Eng., Liquidity Support Facility for Northern Rock Plc (Sept. 14, 2007), *available at* http://www.bankofengland.co.uk/publications/news/2007/090.htm.

123. *Northern Rock*, H.M. TREASURY, http://www.hm-treasury.gov.uk/fin_stability_nr.htm (last visited Oct. 15, 2012).

124. *See* Press Release, Fed. Hous. Fin. Agency, Fact Sheet: Questions and Answers on Conservatorship (Sept. 7, 2008), *available at* http://www.treasury.gov/press-center/press-releases/Documents/fhfa_consrv_faq_090708hp1128.pdf.

125. HONOHAN ET AL., *supra* note 87, at 159, 160.

126. Press Release, Lehman Brothers, Lehman Brothers Holdings Inc. Announces It Intends to File Chapter 11 Bankrupcy Petition; No Other Lehman Brothers' U.S. Subsidiaries or Affiliates, Including Its Broker-Dealer and Investment Management Subsidiaries Are Included in the Filing

across the world tumbled.[127] The markets determined that Anglo Irish Bank was particularly exposed.[128] A March 2008 report by analyst Philip Ingram of Merrill Lynch identified Anglo Irish Bank as the bank with the greatest credit risk to the bursting U.K. commercial-property market.[129] Days later, the Lex column in the *Financial Times* suggested that "nobody wants to have anything to do with banks with commercial property exposure (Anglo Irish Bank and HBOS)."[130] At this stage, investors started to sell their shares in significant numbers.[131]

Interestingly, the management of many of the institutions, the so-called "insiders," did not appear to engage in conduct to push the share prices toward the "correct" price as Manne had predicted. In fact, the signals suggested that the market price represented good value for potential investors as many directors invested heavily in their own firms. For example, between September 2007 and September 2008, David Drumm increased his shareholding in Anglo Irish Bank from 510,899 to 1,013,556 shares. Sean Fitzpatrick increased his holding from 4,512,712 to 4,909,429 shares during the same period.[132] In the twelve months leading up to September 2007, David Drumm had increased his holding by 205,379 shares and Sean Fitzpatrick by 38,843 shares.[133]

The level of takeovers in Europe experienced an upward trend from 2003 to 2007 both in terms of value and number.[134] But it has been a long-acknowledged fact that the discipline of the capital market is only effective within a limited range.[135] John Coffee, commenting on the MCC, pointed out that the level of risk required to accept a financially distressed company is high. Poorly managed companies may be perceived as carrying excessive risk and may thus become indigestible.[136] In other words, these businesses are immune from attack precisely because of their pervasive inefficiency.[137] This was of course true in the aftermath

(Sept. 15, 2008), *available at* http://www.lehman.com/press/pdf_2008/091508_lbhi_chapter11_announce.pdf.

127. Larry Elliot et al., *Nightmare on Wall Street*, GUARDIAN (Sept. 16, 2008), http://www.guardian.co.uk/business/2008/sep/16/marketturmoil.lehmanbrothers.

128. HONOHAN ET AL., *supra* note 87, at 123.

129. Michael Lewis, *When Irish Eyes Are Crying*, VANITY FAIR, Mar. 2011.

130. *European Banks*, FIN. TIMES (Mar. 18, 2008), http://www.ft.com/intl/cms/s/0/8c29bd5a-f48c-11dc-aaad-0000779fd2ac.html#axzz2JIyzfkeG.

131. HONOHAN ET AL., *supra* note 87, at 157.

132. ANGLO IRISH BANK, ANNUAL REPORT & ACCOUNTS (2008), *available at* http://www.irishtimes.com/focus/2009/anglo/index.pdf.

133. ANGLO IRISH BANK, ANNUAL REPORT & ACCOUNTS (2007), *available at* http://www.ibrc.ie/About_us/Financial_information/Archived_reports/Annual_Report_2007.pdf.

134. MARCCUS PARTNERS, *supra* note 28, at 284.

135. Coffee, *supra* note 21, at 1200.

136. *Id.* at 1203, 1204.

137. *Id*. at 1204.

of the crisis.[138] But until 2007–2008, there did not seem to be a public perception that the Irish banks were badly managed. For example, in January 2007, the international management-consultancy firm Oliver Wyman named Anglo Irish Bank "the world's best bank" in the year of 2006.[139]

A further complication for Anglo Irish Bank arose in the form of a significant undisclosed contract for differences (CFD) holding in the company. The Anglo "insiders" described themselves as "physically shocked" when they finally discovered in September 2007 that one of their lending clients, Sean Quinn, had invested in CFDs relating to at least 25% of Anglo's share capital.[140] At the time, neither Irish nor E.U. law required public disclosure of these holdings, and the company was in no better position than the market to identify this "hidden" owner or determine the scale of his holding.

In addition to the failure of the MCC to lead to inefficient companies being taken over, it is argued that the MCC failed in another way. One of the three government-commissioned reports on the banking crisis, the Nyberg Report, was given the express mandate to examine why a number of public and private institutions had acted in an imprudent or ineffective manner during the period spanning January 1, 2003, to January 15, 2009.[141] After discussing the intense market-share competition between domestic and foreign banks and the growth in lending, especially to the property market, Nyberg noted,

> It was against this backdrop that the covered banks pursued strategies which would lead to higher growth, higher reported profits and higher bank valuations. A primary reason appears to have been to prevent a predatory takeover by another bank (either domestic or foreign) and thus maintain independence.[142]
>
> . . .
>
> The strategies of the two bigger banks [Allied Irish Bank and Bank of Ireland] included a desire to maintain their independence. To drive share price growth, and thereby increase their market capitali-

138. Indeed, it has been reported that Irish Nationwide had been on the market since 2007 and that in the hours leading up to the government's guarantee on September 30, 2008, Anglo Irish Bank approached AIB and Bank of Ireland to determine their interest in merging with or acquiring the company. *See* SIMON CARSWELL, ANGLO REPUBLIC: INSIDE THE BANK THAT BROKE IRELAND 193, 214 (2011).

139. Joseph Cotterill, *World's Best Bank (2006 Vintage)*, FIN. TIMES BLOG (Feb. 11, 2011), http://ftalphaville.ft.com/blog/2011/02/11/485311/worlds-best-bank-2006-vintage/.

140. *See* BRIAN CAREY & TOM LYONS, THE FITZPATRICK TAPES 115 (2011).

141. NYBERG, *supra* note 89, at 1.

142. *Id.* at 21. Nyberg concluded that an additional reason in a number of cases was "professional pride and a desire to catch up with or stay ahead of the competition (i.e. playing to win)."

> sations, it was felt that banks needed to show sufficiently strong growth in earnings and at least maintain market share. Strong market capitalisations, in turn, somewhat protected the banks from takeover by a domestic or foreign competitor . . . . Accordingly, during the Period, strategies in both bigger banks evolved to allow increased exposure to the commercial property market as this was a sector that could provide for the significant loan growth required to meet earnings targets.[143]

This finding is particularly troublesome in that it suggests that the MCC, rather than acting as a disciplinary force, acted as a destabilizing force on the management of potentially vulnerable companies.

VI. CONCLUSION

Lord Turner's findings regarding the disciplinary effect of the markets were generally equally negative. He opined:

> But a strong case can be made that the events of the last five years have illustrated the inadequacy of market discipline: indeed, they suggest that in some ways market prices and market pressures may have played positively harmful roles. . . . Bank share prices similarly failed to indicate that risks were increasing, but rather delivered strong market price reinforcement to management's convictions that their aggressive growth strategies were value creative.[144]

This is consistent with research that has demonstrated the existence of regulatory paradoxes where regulation "not only fails to change behaviour, manage risks or achieve any other stated goals, but actually produces the opposite effects from those intended."[145] If, as is argued here, a case can be made that the MCC has negative, or at best neutral, effects on the behavior of corporate boards, further thought needs to be given to the potential effect such a determination has on financial regulation, corporate governance, and takeover regulation. A number of possible scenarios may be considered.

If corporate management acts inefficiently, but the market fails to recognize this fact, the management will not be concerned with a hostile bid because the share price will remain high. The MCC will simply not operate, and regulators seeking to curb agency costs will need to look to other forms of regulation. It is noticeable that credit institutions have become the subject of an increased number of mandatory corporate governance rules. In Ireland, for example, the Central Bank has introduced a

---

143. *Id.* at 24–25.

144. FIN. SERVS. AUTH., *supra* note 72, at 46.

145. Julia Black, *Paradoxes and Failures: 'New Governance' Techniques and the Financial Crisis*, 75(6) M.L.R. 1037, 1039 (2012).

corporate governance code with statutory effect for credit institutions and insurance undertakings.[146] At the E.U. level, new requirements govern the remuneration of certain personnel of credit institutions and investment firms.[147]

Kurt Vonnegut famously observed that "a sane person to an insane society must appear insane."[148] In this context, if management acts efficiently (namely, good corporate governance prevails and sound risk-management systems are applied) but this trait is not valued by the market, the management may correctly be concerned about a takeover from a less scrupulous bidder. Such a bidder may acquire the company and seek to engage in profitable, though not necessarily sustainable, behavior. The perverse effects of the MCC may apply. At present, the Directive, the City Code, and the Irish Takeover Rules allow the target board to mount a robust defense to any action. As such, one might consider that if a board refused to engage in short-term behavior and became the subject of a hostile offer, the board could explain that it was concerned with preserving the long-term value of the company. While this might have some effect in a securities-exchange offer, it would arguably be significantly less persuasive in a cash bid. The company's success in retaining its independence would then depend on persuading shareholders not to accept what may be a sizable premium offer over market price. This may not be easy. Shareholders may not be interested in arguments based on the benefits to the company moving forward.

By way of example, one might consider the hostile takeover of Cadbury PLC by Kraft Foods, Inc. in 2010.[149] Vince Cable, the current U.K. Business Secretary, complained that the decision to sell was made by institutional shareholders whom he referred to as "short term investors and financial gamblers [who] value a quick buck above all else."[150] By the time the offer was finally recommended by the board, hedge funds

---

146. CENT. BANK OF IRELAND, CORPORATE GOVERNANCE CODE FOR CREDIT INSTITUTIONS AND INSURANCE UNDERTAKINGS (2010), *available at* http://www.centralbank.ie/regulation/poldocs/consultation-papers/Documents/CP41%20-%20Corporate%20Governance%20Requirements/Corporate%20Governance%20Paper%20-%204%20November%20%283%29%20Amended%2023%20Feb%202011.pdf; *see* Blanaid Clarke, *Lessons Learned – The Corporate Governance Code For Credit Institutions and Insurance Undertakings*, 33 DUBLIN U. L.J. 172–95 (2011) (festschrift for Chief Justice Ronan Keane).

147. *See, e.g.*, Commission Recommendation on Remuneration Policies in the Financial Services Sector 2009/384, 2009 O.J. (L 120) 22.

148. *See* KURT VONNEGUT, WELCOME TO THE MONKEY HOUSE (1968).

149. Blanaid Clarke, *Directors' Duties in a Changing World: Lessons from the Cadbury Plc Takeover*, 7 EUR. COMPANY L. 204 (2010).

150. Press Release, Dep't for Bus. Innovation & Skills, Cable Calls for Long Term Focus for Corporate Britain (Sept. 22, 2010), *available at* http://news.bis.gov.uk/content/Detail.aspx?ReleaseID=415572&NewsAreaID=2.

and other short-term investors owned almost 31% of the company's shares, up from just 5% before the offer was made.[151] Sir Roger Carr, the Cadbury Chairman, commented that once it became clear that the company would not remain independent, his task was to achieve the highest selling price for shareholders.[152] This position was not altered by § 172 of the U.K. Companies Act 2006,[153] which ostensibly promotes corporate social responsibility by obliging directors to be aware of the likely consequences of any decision in the long term, the interests of the company's employees, and the impact of the company's operations on the community and the environment.[154] In June 2011, an independent review was established under the chairmanship of Professor John Kay to consider whether U.K. equity markets provided sufficient support for British industry's capacity for innovation, its brands and reputations, and the skills of its workforce. In an interim review, Kay noted that in its survey of market participants, "there was wide agreement that the ability to mount a successful takeover now depends almost solely on the capacity and inclination to offer sufficient premium to the likely share price in the absence of the bid."[155]

The final report (Kay Report) similarly referred to the role of short-term arbitrageurs whose sole purpose is to gamble on the bid being accepted, and noted:

> If there is a problem, it is that the underlying holders of shares are unwilling to reject an immediate offer at a premium to the previous share price even if they believe that the still higher fundamental value of the share will be revealed in the long-run. Or that they have no idea of the fundamental value of the share, but take the money and run.[156]

---

151. Roger Carr, *Cadbury: Hostile Bids and Takeovers*, UNIV. OF OXFORD (Feb. 15, 2010), http://www.sbs.ox.ac.uk/newsandevents/previousevents/Pages/RogerCarrCadbury.aspx.

152. *Id*.

153. Companies Act, 2006, c. 46, § 172 (U.K.). Section 172(1) of the Companies Act 2006 provides that a director must "act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole."

154. *See* Andrew Keay, *Shareholder Primacy in Corporate Law: Can It Survive? Should It Survive?*, 7 EUR. COMPANY & FIN. L. REV. 69 (2010); Andrew Keay, *Tackling the Issue of the Corporate Objective: An Analysis of the United Kingdom's 'Enlightened Shareholder Value Approach,'* 29 SYDNEY L. REV. 577 (2007).

155. *See* TOM KAY, THE KAY REVIEW OF UK EQUITY MARKETS AND LONG-TERM DECISION MAKING: INTERIM REPORT (2012), *available at* http://www.bis.gov.uk/assets/biscore/business-law/docs/k/12-631-kay-review-of-equity-markets-interim-report.pdf.

156. *Id.* at 61. The Kay Review suggested that the development of stewardship activity by asset managers is "the best – and probably the only – effective check on such actions." It also advised the U.K. government to adopt a more active approach toward companies planning major acquisitions of U.K. businesses and to take a negative view of a transaction only in cases where at least one of the

The Government responded positively to the Kay Report and accepted its recommendation that "the scale and effectiveness of merger activity of and by UK companies should be kept under careful review" by the Department for Business Innovation and Skills and by companies themselves.[157] It also endorsed the call in the Kay Report's "Good Practice Statement for Company Directors" to "acknowledge that long-term value creation in the interests of shareholders is best served by strategies which focus on investing appropriately to deliver sustainable performance rather than treating the business as a portfolio of financial interests."[158]

Klaus Hopt has described the MMC for banks as "especially weak" noting that it "cannot be trusted to be a major disciplining force in bank corporate governance."[159] While the Irish banking crisis has demonstrated weaknesses in the MCC, it must be acknowledged that the overvaluation of credit institutions by the markets prior to the crisis does not justify discounting the theory completely. Demsetz's nirvana fallacy[160] warns against such a step. Similarly, Kuhn, the influential philosopher, has cautioned against imprudent abandonment of a theory simply because an anomaly is present in its supporting data.[161] Though one might argue that the crisis has shown other forms of corporate governance and regulation to be imperfect, the MCC might still be considered an important weapon in the agency-problem armory. We have accepted other limitations to the theory in the past, and this may just be another one to factor into our thinking.

---

following conditions was fulfilled: "the acquirer appeared to have significantly less capacity to manage the business than the existing management team; the combined concern appeared likely to be substantially weaker financially than the existing UK business; a probable consequence of the transaction was a material loss of high level functions, or of employment from the UK."

157. DEPARTMENT FOR BUSINESS INNOVATION AND SKILLS, ENSURING EQUITY MARKETS SUPPORT LONG TERM GROWTH: THE GOVERNMENT RESPONSE TO THE KAY REVIEW 21 (2012), *available at* http://www.bis.gov.uk/assets/biscore/business-law/docs/e/12-1188-equity-markets-support-growth-response-to-kay-review.

158. *Id.* at 21.

159. Klaus Hopt, *Corporate Governance of Banks After the Financial Crisis*, *in* FINANCIAL REGULATION AND SUPERVISION, A POST-CRISIS ANALYSIS 342 (Eddy Wymeersch, Klaus Hopt & Guido Ferrarini eds., 2012).

160. Demsetz explains this concept as follows: "The view that now pervades much public policy economics implicitly presents the relevant choice as between an ideal norm and an existing 'imperfect' institutional arrangement. This *nirvana* approach differs considerably from a *comparative institution* approach in which the relevant choice is between alternative real institutional arrangements." *See* H. Demsetz, *Information and Efficiency: Another Viewpoint*, 12 J. L. & ECON. 1, 1 (1969).

161. THOMAS S. KUHN, THE STRUCTURE OF SCIENTIFIC REVOLUTION 81 (1970).