

The background to the reference

4.1. Lonrho held by July 1977 29.25 per cent of the issued share capital of Scottish and Universal Investments Limited (SUITS) which at that time held 10.29 per cent of the issued share capital of House of Fraser. In April 1978 Lonrho made a public offer for the remainder of the issued share capital of SUITS which, if accepted, would have increased Lonrho's direct holding in House of Fraser to between 29 and 30 per cent. These mergers were referred to the Commission whose report (the SUITS report¹) concluded that, although there would be some risk of detriment to the public interest, the degree of risk would not be sufficiently great for a finding that the acquisition of SUITS might be expected to operate against the public interest. The Commission also concluded that the merger situation created in respect of Lonrho and House of Fraser might be expected not to operate against the public interest but added that this conclusion was confined to the step then contemplated (which would result in Lonrho acquiring ability materially to influence the policy of House of Fraser) and a new situation would be created if Lonrho sought to acquire control of House of Fraser.

4.2. At this stage the House of Fraser Chairman was Sir Hugh Fraser, and Lord Duncan-Sandys and Mr Rowland of Lonrho (referred to as 'the minority directors') had become members of the Board, the latter as Deputy Chairman. In August 1980 the Board appointed Professor Roland Smith and Mr Ernest Sharp as directors and the former as Deputy Chairman in place of Mr Rowland. At the same time an Executive Committee of the Board was formed with Professor Smith as Chairman and without Lonrho representatives. On 28 January 1981 the Board terminated Sir Hugh Fraser's appointment as Chairman (he resigned from the Board in February 1982) and appointed Professor Smith in his place. On the same day Lonrho announced an offer of 150p per share for the House of Fraser shares it did not already own and the proposed merger was referred to the Commission. The Commission's report (the 1981 report²), to which we refer in paragraph 4.3, contains a full account of what it describes as 'the acrimonious nature of the disputes between Lonrho and House of Fraser' which took place during the period between March 1979 and February 1981 (paragraph 4.11), pointing out that there was little agreement between the two parties as to the rights and wrongs of the disputes or their relevance to the inquiry. We encountered a similar situation in the present inquiry.

4.3. The 1981 report concluded, with one dissident, that the proposed merger might be expected to operate against the public interest. On 15 December 1981 Lonrho gave undertakings to the Secretary of State (the 1981 undertakings) that it would not, by itself or with persons associated with it, seek to increase its shareholding or their total shareholding to 30 per cent or more. At the same time the Department of Trade confirmed that the undertakings did not affect

¹ A report on the proposed merger of Lonrho and Scottish and Universal Investments and on the resulting merger situation between Lonrho and House of Fraser Limited (HC 261 published on 15 March 1979).

² A report on the proposed merger of Lonrho Limited and House of Fraser Limited (HC 73 published on 9 December 1981).

the normal rights of Lonrho as a shareholder and that the Government would be prepared to consider at any time representations from Lonrho that in the light of new circumstances Lonrho should be released from the undertakings or that the undertakings should be changed. The undertakings and the Department's letter are reproduced as Appendices 9 and 10. House of Fraser was informed that, if Lonrho sought release from its undertakings, House of Fraser would be given the opportunity to make full representations.

4.4. Throughout the period from that time on relations between Lonrho and House of Fraser continued to be acrimonious. The conflict was expressed in a flow of correspondence, telex and telephone communications between the parties; at Board meetings, in circulars to shareholders and statements to the press; at Annual and Extraordinary General Meetings frequently involving polls and proxy battles; and in litigation before the Courts in Scotland.

4.5. It may be revealing of the attitude of each side to the other that Counsel for House of Fraser, commenting on a suggestion about negotiation on a particular matter between the two sides, told us that it 'presupposes a relationship between House of Fraser and Lonrho which does not exist. The fact is that the years have taken their toll'. Similarly, Counsel for Lonrho, commenting on Lonrho's making the Harrods demerger issue a matter of public debate instead of bringing it to the House of Fraser Board first (see paragraph 4.8), said that this was an 'odd Board and it inevitably generated odd behaviour, or unusual behaviour, by Lonrho'. We do not think it would be helpful to attempt to set out a comprehensive record of the events and incidents of this conflict. We summarise below some of the principal events, mostly relating to general meetings and legal proceedings over the period, as background to the reference. We later refer to aspects of the conflict in Chapter 5.

4.6. On 26 January 1982, barely six weeks after giving the undertakings, Lonrho wrote to the Secretary of State asking for discussions with the Department of Trade about release from the undertakings. After a meeting with Lonrho, the Secretary of State referred the matter to the Office of Fair Trading (OFT) for advice and both Lonrho and House of Fraser submitted representations. On 16 September 1982 Lonrho stated that 'it would not wish in the present circumstances to renew its bid for House of Fraser as it believes the current stock market values do not reflect the realities of the present unsatisfactory level of profitability since Lonrho's offer for House of Fraser'. Lonrho requested that its application should be allowed to lie on the table to await further developments and, in the interim, should not be proceeded with but should not be formally withdrawn. On 22 October 1982 the OFT indicated that, although Lonrho had not withdrawn its request, the Director General of Fair Trading did not propose to treat Lonrho's application for release from its undertakings as still current and in all the circumstances he had come to the view that it would not be appropriate at the present time to tender advice to the Secretary of State.

4.7. At the Annual General Meeting on 24 June 1982 the House of Fraser Board put forward (to take account, House of Fraser told us, of recent changes in the Companies Acts) an ordinary resolution to authorise it to allot unissued

shares and two special resolutions, one to disapply certain pre-emption rights and the other to adopt new Articles of Association. Lonrho requisitioned two ordinary resolutions, one to make any authority conferred on the directors as to allotment of shares conditional on the prior sanction of the company in general meeting, and the other to request the directors to ensure that the company's ordinary shareholders should be given the opportunity to consider any offer made for their shares from any source. The Board's ordinary resolution conferring authority on the directors to allot unissued shares was carried on a vote of 64.1 million for and 57.2 million against. The Lonrho ordinary resolutions were defeated on votes of 57.2 million and 57.1 million for and 65.4 million against. Lonrho voted against the Board's two special resolutions and since these required a 75 per cent majority they were not passed.

4.8. In addition to its statement of 16 September 1982 referred to in paragraph 4.6, on the same day Lonrho notified the House of Fraser Board without prior consultation (and released the information to the Press¹) that it proposed to requisition an Extraordinary General Meeting to consider resolutions relating to the demerger of Harrods and the removal of Professor Smith both as a director and as Chairman of House of Fraser. At the meeting which was held on 4 November 1982 the latter resolution was not put. The former requested the Board to formulate proposals for the demerger of Harrods into a separate public company the shares of which would be held *pro rata* by the existing shareholders of House of Fraser and to convene an Extraordinary General Meeting within 90 days to consider the demerger proposals and such advice as the Board might wish to give. The Board stated that, since it was already investigating the possibility of demerger, it was immaterial whether the resolution was passed or not. In the event, it was carried on a poll by 72.4 million votes for with 31.3 million against and 26.3 million abstentions.

4.9. At a special Board meeting on 31 March 1983 to consider the report on demerger of a Working Party which had been set up in September 1982 it was decided (the minority directors dissenting) that demerger would materially harm the interests of House of Fraser, its shareholders and employees. A resolution was accordingly moved at an Extraordinary General Meeting called for 6 May 1983 accepting the recommendation of the Board that Harrods should remain in the House of Fraser group and expressing confidence in the Board and this was carried by 65.6 million votes to 63.8 million. Following the decision to call that Extraordinary General Meeting Lonrho requisitioned another such meeting to consider a resolution on the demerger issue alone and this was fixed to be held immediately after the Annual General Meeting on 30 June 1983.

4.10. At this Extraordinary General Meeting Lonrho proposed an ordinary resolution approving demerger. The House of Fraser Board proposed a special resolution to alter the Memorandum of Association which it said it had been advised was an essential pre-condition of a tax-efficient demerger. Lonrho did not accept the necessity for such a resolution. House of Fraser Board recommended shareholders to vote against both resolutions. The ordinary resolution was carried on a vote of 68.2 million in favour and 63.4 million

¹ See footnote (1) to paragraph 5.13.

against. There were 67.5 million votes in favour and 64 million against the special resolution, the votes in favour thus falling short of the required majority of 75 per cent by 23.7 per cent. Professor Smith in a letter to House of Fraser shareholders stated that, in the light of the defeat of the special resolution the Board regarded the demerger debate as over. Lonrho called upon the Board, in view of the passage of the ordinary resolution, to put forward detailed proposals for demerger or give way to directors who would.

4.11. During this period, there have been four separate sets of proceedings in the Scottish Courts involving House of Fraser (or its Board) and the minority directors, none of which has yet to come to trial. Interdict proceedings were commenced by House of Fraser against the minority directors on 20 April 1983 to prevent the use of the House of Fraser logo by the minority directors in circulars to House of Fraser shareholders concerning demerger and to rule invalid proxy cards attached thereto. The Court declined to order any interim interdict because it did not anticipate any real likelihood of confusion in the minds of shareholders. On 25 April 1983 the minority directors brought an action to restrain the House of Fraser Board from bringing forward to 26 April a Board meeting previously planned for 28 April at which the 1982-83 report and accounts were to be considered. The Court granted an interim interdict restraining the bringing forward of the meeting but declined to order that it be put off to 30 April as sought by the minority directors. On 18 August 1983 the minority directors instituted proceedings seeking a declaration that in their capacity as House of Fraser directors they were entitled to inspect proxies, pollcards and instruments appointing proxies relating to the Extraordinary General Meetings on 6 May and 30 June 1983. No hearing has yet taken place. On 18 November 1983 the minority directors commenced proceedings against House of Fraser for an interdict to prevent House of Fraser approving or sanctioning capital expenditure or entering into contracts without first providing to the Board all the necessary information to enable the Board to give due and proper consideration to such expenditure. On 23 November 1983 the Court declined to grant an interim interdict.

4.12. On 23 August 1983, following a request by House of Fraser for investigation of the membership of the company on the grounds that certain shareholders had acquired their holdings recently to act in concert with Lonrho (undisclosed 'concert parties' being an offence under the Companies Act 1981), Mr John Griffiths QC was appointed as Inspector by the Secretary of State for Trade and Industry under section 172 of the Companies Act 1948 to inquire into the membership of House of Fraser. The Inspector extended his enquiries in December 1983 following allegations by Lonrho about the existence of a 'concert party' comprising a number of institutions and other persons connected with House of Fraser and alleged to be opposed to Lonrho. The Inspector's report (the Griffiths report) was published on 9 August 1984. He found that no 'concert party' had been proved. The Inspector described his report as an 'interim' report because he had not been able to reach any final conclusion about a holding of 2 million shares which were the subject of restrictions ordered by the Scottish Courts. The Secretary of State decided not to ask Mr Griffiths to make further enquiries about those shares on the ground that the cost and effort would not be justified.

4.13. Meanwhile, on 16 May 1984 Lonrho requisitioned resolutions to be put before the next Annual General Meeting of House of Fraser to increase the maximum number of directors from 18 to 25 and appoint 12 named individuals¹ to the Board, six of whom were directors of Lonrho. Lonrho stated that the purpose of the resolutions was to ensure that the issue of demerger was fairly put to shareholders, not to alter permanently the composition of the Board or to increase or consolidate Lonrho's position in House of Fraser. Lonrho said that it would concur in a reconstruction of the Board when the issue of demerger had been resolved. On 31 May 1984 the Secretary of State made the present merger reference.

4.14. On 1 June 1984 Lonrho requisitioned further resolutions for the next House of Fraser Annual General Meeting. These were (a) to appoint four additional directors (being four of the six non-directors of Lonrho named in the requisition of 16 May 1984), conditionally upon the resolutions in the earlier requisition being withdrawn, not put or defeated; and (b) to direct the directors of House of Fraser not, *inter alia*, to enter into any contract or arrangement which would prejudice the issue of demerger of Harrods pending the outcome of the Secretary of State's reference to the Commission. The resolutions in (b) were subsequently withdrawn by Lonrho and replaced by requisitioned resolutions to request the directors of House of Fraser to the like effect.

4.15. On 4 July 1984 Lonrho gave interim undertakings to the Secretary of State to withdraw those parts of the requisitions which proposed the enlargement of the Board and the appointment of additional directors (other than two directors of Lonrho, Mr Robinson and Mr Spicer) and not to vote against the re-election as a director and/or Chairman of Professor Smith. At the subsequent Annual General Meeting, which was held on 28 September (and at which Lonrho opposed Mr Sharp's re-election and supported the election of Mr Robinson and Mr Spicer), the resolutions relating to Harrods were carried and Mr Rowland, Professor Smith and Mr Sharp were re-elected, but Mr Robinson and Mr Spicer were not elected.

4.16. On 2 November 1984 Lonrho sold its 46,098,800 shares (29.9 per cent of the issued ordinary capital) in House of Fraser to Alfayed Investment and Trust (UK) Ltd. During the following week it purchased 7 million shares and sold a further 750,000. Between 22 and 30 November Lonrho purchased a further 3,500,000 shares which increased its shareholding to approximately 6.3 per cent. Included in the shares purchased were shares previously held by shareholders who were believed by House of Fraser to have been supporters of Lonrho (see paragraph 6.14). Lonrho's explanation of the reasons for its recent transactions in House of Fraser shares is contained in paragraph 6.21.

4.17. On 7 November 1984 Lonrho informed us that it had abandoned the particular proposals made in the resolutions requisitioned on 16 May 1984 and had no present intention of reviving such proposals. It said that its intention to bid for House of Fraser had not been abandoned and it had recently

¹ The individuals were Sir Edward du Cann, Mr A H Ball, Mr R F Dunlop, Mr T J Robinson, Mr P G B Spicer, Mr R E Whitten (directors of Lonrho) and Mr R W Aitken, Mr G R A Copus, Mrs J d'Abo, Sir Hugh Fraser, Mr A C Gilmour and Lord Roger Manners.

indicated to the Secretary of State that it wished to be released from the undertakings it gave in 1981. On 22 November 1984 Lord Duncan-Sandys and Mr Rowland resigned from the House of Fraser Board with effect from 31 December 1984. On 3 January 1985 Mr Mohamed Al-Fayed and Mr Ali Al-Fayed were appointed directors of the company.