THE CITY OF LONDON LAW SOCIETY
COMPANY LAW COMMITTEE

Agenda

for the 270th meeting
at 10:30 a.m. on Tuesday, 22 July 2014
at Slaughter and May, One Bunhill Row, EC1Y 8YY
(Tel: 020 7600 1200; Fax: 020 7090 5000)

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1. Welcome and apologies

Attending: William Underhill (chairman); Peter Wilson (secretary); Robert Boyle; Michael Hatchard; Rob Hutchings (alternate for Martin Webster); Simon Jay; Vanessa Knapp; Stephanie Maguire (alternate for Mark Austin); Stephen Mathews; Maegen Morrison (alternate for Andrew Pearson); James Palmer; Kath Roberts (alternate for David Pudge); Patrick Speller; Jeffrey Sultoon (alternate for Nicholas Holmes); Victoria Younghusband.

Apologies: Nicholas Holmes; Chris Horton; Andrew Pearson; David Pudge; Richard Spedding; Keith Stella.

2. Approval of minutes

The Chairman noted that draft minutes for the meeting held on 20 May 2014 will be circulated for comment in due course.

3. Matters arising

3.1 MAD II and Market Abuse Regulation

The Committee noted that, on 12 June 2014, Regulation (EU) No. 596/2014 on market abuse (MAR) and Directive 2014/57/EU on criminal sanctions for market abuse and insider dealing (CSMAD) had been published in the Official Journal.

3.2 ESMA consultations on MAR implementation

The Committee noted that, on 15 July 2014, ESMA had published a consultation paper on draft technical standards relating to MAR (the "**Technical Standards CP**"), and a consultation paper on draft technical advice to the EC on possible delegated acts concerning MAR. The deadline for responses to both consultations is 15 October 2014.

Committee members raised various concerns regarding the proposals in the Technical Standards CP, including the following:

- ESMA does not seem to have accepted the Market Abuse Joint Working Party's previous comment (in its response to ESMA's November 2013 discussion paper on possible implementing measures under MAR) that the market soundings

regime under MAR provides a safe harbour, and accordingly compliance with that regime's detailed requirements is not mandatory.

- ESMA has rejected the argument that if a market sounding does not involve disclosure of inside information, then there is no basis for ESMA to regulate that communication.

- Where a financial adviser or broker undertakes market soundings on an issuer's behalf, the issuer should not have to duplicate the steps taken by its financial adviser or broker in order to take advantage of the safe harbour.

- Where an issuer wishes to undertake market soundings itself, it should not have to put in place internal arrangements akin to those required by financial institutions, e.g. recorded lines.

- ESMA's proposed content requirements for insider lists include information which issuers would not normally hold regarding their employees, seem disproportionate, and may go beyond what is permitted under the Data Protection Act 1998.

The Committee agreed that the Market Abuse Joint Working Party should be asked to respond to ESMA's two consultation papers. Ideally the Joint Working Party's response to the Technical Standards CP would include suggested drafting changes to address its concerns.

It was also suggested that the Joint Working Party liaise with the GC100 and EuropeanIssuers regarding its concerns.

3.3 FRC guidance on the Strategic Report

The Committee noted that, on 9 June 2014, the FRC had published its final Guidance on the application of the strategic report requirements introduced by the Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013 and a related feedback statement.

The Committee noted that, on the same date, the FRC had published a letter from BIS to the FRC dated 30 April 2014. In this letter, BIS expressed the view that the liability safe harbour in section 463 of CA 2006 was not intended to protect "inappropriately large volumes of information, including that not required to meet a specific legal requirement" which may have been placed in the reports subject to the safe harbour. BIS indicated that, if this "manifests itself in such a way that it detracts from clear and concise reporting, then the Department [BIS] may need to revisit the operation of the safe harbour provision in future."

The Chairman had questioned this approach with BIS. He was informed that BIS did not intend to suggest that directors' reports can only contain what is legally required, and nothing more. However, the Committee noted that the safe harbour was intended to facilitate frank and fulsome disclosures, and the BIS letter was not helpful.

3.4 Law Commission report on fiduciary duties of investment intermediaries

The Committee noted that, on 1 July 2014, the Law Commission had published a report on fiduciary duties of investment intermediaries, which included a helpful statement of law and guidance for pension trustees.

The Committee noted with approval the report's conclusion that the law of fiduciary duties should not be reformed by statute.

3.5 Response to ESMA consultation paper on draft Regulation under revised Transparency Directive

The Committee noted that a response to this ESMA consultation paper had been submitted by the Listing Rules Joint Working Party of the Company Law Committees of the Law Society of England and Wales and the City of London Law Society.

3.6 Response on proposed changes to Shareholder Rights Directive

The Committee noted that a response on the proposed changes to the Shareholder Rights Directive had been submitted by the Listing Rules Joint Working Party of the Company Law Committees of the Law Society of England and Wales and the City of London Law Society.

3.7 Response to FRC consultation paper on UK Corporate Governance Code

The Committee's response to this FRC consultation paper was noted.

3.8 "Transparency & Trust" – possible prohibition on corporate members of LLPs

An update was provided to the Committee regarding the current position in relation to BIS' possible prohibition on corporate members of LLPs.

3.9 UKLA Liaison Group

The Chairman noted that the UKLA Liaison Group will meet on 28 July. Numbers would be limited. Any Committee members interested in attending were asked to let the Chairman know as soon as possible.

The Chairman noted that the meeting agenda already includes the *Hannam* decision, and the ABI's proposals regarding possible improvements to the IPO process. (These matters are discussed in paragraphs 4.2 and 4.3 below.)

Some Committee members suggested additional agenda items regarding:

- The implications of MAR, and the UKLA's plans in this regard. Transitioning to MAR may be complicated for issuers, and existing UKLA guidance may also need to be amended or withdrawn in light of MAR implementing measures or ESMA guidance. If the UKLA has not already started to consider these issues, then it may be helpful to encourage them to do so.

- Timing of eligibility decisions for new applicants. This issue was discussed at the Committee meeting on 25 March 2014.

The Chairman agreed to ask the UKLA to consider adding these to the agenda.

4. Discussions

4.1 Small Business, Enterprise and Employment Bill

The Committee noted that, on 25 June 2014, the Government had introduced the Small Business, Enterprise and Employment Bill to Parliament. The Committee discussed Parts 7 and 9 of the Bill, which include amendments to the CA 2006 and the Company Directors Disqualification Act 1986 to implement the proposals set out in the Government's response to BIS' "Transparency & Trust" discussion paper.

The Committee also noted that, on 18 July 2014, the House of Commons Public Bill Committee had published a request for written evidence on the Bill. Evidence must be received by 6 November 2014 or, if earlier, the date that the Public Bill Committee concludes its proceedings.

4.2 *Hannam v The Financial Conduct Authority* [2014] UKUT 233 (TCC)

The Committee noted that the upcoming UKLA Liaison Group meeting will discuss the implications for disclosure obligations of the Upper Tribunal's decision in *Hannam*.

The Tribunal had held that Mr Hannam, then Global Co-Head of UK Capital Markets at J.P. Morgan Cazenove, had engaged in the market abuse offence of improper disclosure in breach of section 118(3) of FSMA 2000.

Some concerns were expressed regarding the Tribunal's finding that the standard of proof in market abuse cases is the civil standard of a "balance of probabilities" and not the criminal standard of "beyond reasonable doubt". It was suggested that this finding was contrary to EU case law in a fines context. It was noted that the Tribunal's judgment had not cited any EU cases on this point.

The Committee engaged in a general discussion of the potential implications of *Hannam* in relation to DTR 2. Amongst other matters, the Committee noted two aspects of the judgment which appeared to be inconsistent with current FCA policy and practice:

- The FCA's position up until now has been that the "reasonable investor" test in section 118C(6) of FSMA 2000 provides an exhaustive definition of when information is sufficiently price sensitive to constitute inside information. The Tribunal disagreed. It regarded the likely effect on the price of listed securities as something to be taken into account in assessing whether a reasonable investor would use the information for its investment decisions. The Tribunal took the view that for the purposes of judging the price effect of information, "likely" means that there must be a real (and not fanciful) prospect of the information having an effect on the price of the securities. The Tribunal rejected the argument that "likely" meant "more probable than not" or "may well".

- The Tribunal held that it was reasonable for Heritage to delay announcement of its drilling results (under DTR 2.5.1R) until it could provide information that avoided the risk of misleading the market, i.e. until more definitive results were available. This contrasts with DTR 2.5.5G, which essentially states that the FCA considers delay under DTR 2.5.1R is unlikely to be justified in circumstances other than those described in DTR 2.5.3R or DTR 2.5.5AR. It is also inconsistent with DTR 2.2.9G(2), which generally requires issuers faced with an unexpected and significant event to issue a holding announcement.

  The Tribunal also said that, unless there is some exceptional event or fact that requires immediate disclosure, a listed company could reasonably delay announcing its results until the planned publication date. However, Committee members expressed differing views as to whether it would be safe to rely on this particular aspect of the judgment.

The majority of Committee members thought that, in most cases, it would be safest for law firms to continue to advise their clients based on the FCA's position as stated in DTR 2.5.5G and DTR 2.2.9G(2). The FCA was likely to enforce DTR 2.5.1R on this basis. While it was possible that a client would prevail in a subsequent appeal to the Upper Tribunal, a client is only likely to be willing to take this risk in rare situations.

Nevertheless, the Committee agreed that the FCA should be encouraged to reconsider its DTR 2.5.1R enforcement policy and guidance (in DTR 2.5.5G and DTR 2.2.9G(2)) in light of *Hannam*. This issue should be raised at the upcoming UKLA Liaison Group meeting. For this purpose, the Chairman thought it would be helpful if the UKLA could be provided with examples of issuers which have announced a matter because they believe this is required by DTR 2, but the announcement has prejudiced the issuer's legitimate interests (i.e. the DTR 2.5.1R safe harbour should have applied).

4.3 <u>IPO blackout periods / prospectus availability</u>

The Committee noted that the upcoming UKLA Liaison Group meeting will discuss the ABI's proposals (in its July 2013 report on "Encouraging equity investment") regarding pre-IPO research blackout periods and when the prospectus is made available.

The ABI report recommended action to encourage the early release of pre-IPO research reports, ideally at the same time the prospectus is issued. The ABI indicated that this was likely to require clarifying COBS 12.2.12G, which refers to blackout periods. The Committee noted that a UKLA Technical Note (on the PD Advertisement regime, UKLA/TN/604.1) also refers to blackout periods. The FCA / UKLA's position is that both COBS 12.2.12G and the UKLA Technical Note are just guidance, and they do not make blackout periods mandatory. However, investment banks are unwilling to remove blackout periods while FCA / UKLA guidance still refers to them.

The ABI report also recommended that a UKLA-approved IPO prospectus, which is complete apart from pricing or price range and related information, be issued at least one week earlier than the pathfinder or price range prospectus is currently issued. The ABI considered that this would give investors more time to digest the prospectus.

The Chairman asked Committee members to consider whether any other matters raised in the ABI report would be worth discussing with the UKLA.

5. Recent developments

5.1 Company Law

The Committee noted that, on 11 June 2014, the Companies (Striking Off) (Electronic Communications) Order 2014 had been made. This came into force on 11 July 2014.

5.2 Corporate Governance

The Committee noted that, on 29 May 2014, the Institutional Investor Committee (made up of representatives from the ABI, IMA and NAPF) had published guidance for Audit Committees on what UK institutional investors expect in relation to the audit tendering process.

The Committee noted that, on 1 July 2014, the Secretary of State for Business, Innovation and Skills had launched an Enhanced Voluntary Code of Conduct for executive search firms to encourage more women appointments to FTSE 350 boards.

5.3 Reporting and Disclosure

The Committee noted that, on 10 July 2014, ESMA had published its final guidelines on the enforcement of financial information provided by issuers in accordance with the Transparency Directive. The guidelines will become effective two months after their publication on ESMA's website.

5.4 Public M&A

PCP 2014/1

The Committee noted that, on 16 July 2014, the Code Committee had published PCP 2014/1, which contains miscellaneous proposed amendments to the Takeover Code. The deadline for responses is 12 September 2014. The Takeovers Joint Working Party is gathering comments on this consultation paper with a view to drafting a response.

Updating profit forecasts

Some Committee members expressed concerns regarding the impact of Rule 28.1 of the Takeover Code on some recent takeovers. It is common practice in some jurisdictions (e.g. the US) for companies to provide regular "earnings guidance" statements or other forward-looking profit information. Where a target or securities exchange bidder (or potential bidder) has previously issued such an ordinary course profit forecast, it may be necessary to update this during an offer period to reflect the company's recent financial performance. On some recent takeovers, the Panel has strictly enforced the Rule 28.1 requirements for such a company to obtain reports from its accountants and financial advisers, and to include these in the update announcement. However, delaying the announcement in order to obtain these reports

may put the company in breach of its legal obligations to promptly update the market regarding changes to its previous profit forecast.

It was suggested that, in such situations, the company should be permitted to promptly announce its updated profit forecast, and subsequently release the reports from its accountants and financial advisers when these are available. The Committee agreed that the Panel should be asked to consider amending Rule 28.1 to permit this.

Possible proposals regarding takeovers threatening the national interest

The Committee noted that, on 13 July 2014, the press reported that the Secretary of State for Business, Innovation and Skills had proposed additional measures to protect against foreign takeovers that threaten the national interest. The proposed measures appear to comprise: (a) requiring bidders to adhere to the commitments they make in relation to a takeover in all circumstances, by removing the exception in Note 3 on Rule 19.1 for "material changes of circumstances"; (b) introducing "tough financial penalties" for bidders which fail to honour their commitments; and (c) allowing the Government to intervene in takeovers on "public interest" grounds as a "last resort" where bidders refuse to undertake satisfactory commitments to protect the national interest.

Some Committee members thought it likely that proposals (a) and (b) would discourage bidders from giving commitments. Others were concerned that proposals along these lines would prove unworkable in practice.

In relation to proposal (c), the Committee noted that, if the proposed intervention power were to apply to European takeovers, then it would need to be compatible with European law requirements regarding the free movement of capital. This would be a very significant constraint.

The Committee agreed to monitor developments in this area.

5.5 Equity Capital Markets

The Committee noted that, on 12 June 2014, HM Treasury, the Bank of England and the FCA had announced the Fair and Effective Financial Markets Review and published its terms of reference. The review will produce a consultation document in Autumn 2014 and a final report by June 2015.

The Committee noted that, on 9 July 2014, the FCA had published a consultation paper to review competition in the wholesale securities and investments sector. The paper includes a section titled "Cost of equity and debt underwriting". The deadline for responses is 9 October 2014.

5.6 Accounting

The Committee noted that, on 4 June 2014, the FRC had published a paper confirming that the presentation of a true and fair view remains a fundamental requirement of financial reporting under IFRS and UK GAAP.

The Committee noted that, on 16 June 2014, ESMA had published a report of its review of the application of accounting requirements for business combinations in IFRS financial statements.

5.7 Europe

The Committee noted that, on 12 June 2014, Directive 2014/65/EU on markets in financial instruments (MiFID II) had been published in the Official Journal. MiFID II entered into force on 2 July 2014, and Member States must implement most of its provisions by 3 January 2017.

The Committee noted that, on 25 June 2014, the European Commission had launched an online consultation on the third country equivalence mechanism, process and equivalence criteria in relation to Chapter 10 of the Accounting Directive (2013/34/EU). The deadline for responses is 10 October 2014.

The Committee noted that, on 22 May 2014, Directive 2014/51/EU (Omnibus II Directive) had been published in the Official Journal. The Directive entered into force on 23 May 2014, and Member States must implement it by 1 January 2016.

The Committee noted that, on 27 May 2014, Directive 2014/56/EU amending the Statutory Audit Directive and Regulation (EU) No. 537/2014 regarding the statutory audit of public interest entities had been published in the Official Journal. Both the Directive and the Regulation entered into force on 16 June 2014. The Regulation will apply in Member States from 17 June 2016 (other than the Article 16(6) prohibition on "Big Four only" clauses, which applies from 17 June 2017). Member States must implement the Directive by 17 June 2016.

The Committee noted that, on 9 July 2014, the European Commission had published a white paper titled “Towards More Effective EU Merger Control”.

5.8 Cases

The Committee noted the judgments in:

- *The Registrar of Companies v Swarbrick and others (as Joint Administrators of Gardenprime Limited (in Administration))* [2014] EWHC 1466 (Ch)

- *Emirates Trading Agency LLC v Prime Mineral Exports Private Limited* [2014] EWHC 2104 (Comm)

- *Smithton Limited v Guy Naggar* [2014] EWHC 1466 (Ch)

The Committee noted that, in *Smithton*, the Court of Appeal agreed with the proposition that there was no one definitive test for a *de facto* director. However, paragraphs 33 to 45 of the judgment usefully set out a number of points which are of general practical importance in determining who is a *de facto* director of a company.