

# CLIENT UPDATE

## FCA PUBLISHES PROPOSALS ON CHANGES TO THE PREMIUM LISTING RULES, WITH FOCUS ON COMPANIES WITH A CONTROLLING SHAREHOLDER

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### OVERVIEW

On November 5, 2013, the FCA published a further Consultation Paper containing updated proposals on changes to the UK Listing Rules focusing on premium listed companies with controlling shareholders. The Consultation Paper (CP 13/15) contained its views on responses to an earlier consultation published in October 2012 (CP 12/25)<sup>1</sup> in the form of new draft “near-final” rules (on which the FCA is not inviting further comment), as well as some new proposals for further consultation.

The draft amendments to the Listing Rules will impose new requirements on such controlled companies regarding, *inter alia*, specified agreements with controlling shareholders and the election process for independent directors. The FCA is also consulting on potential sanctions for breach of agreements with controlling shareholders, as well as a requirement for additional independent shareholder approval where such a company seeks to cancel its premium listing or transfer to a standard listing.

The key elements of the FCA’s proposals in CP 13/15 (which is available [here](#)) are summarized below. Once the new rules are in force, new applicants for a premium listing with controlling

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<sup>1</sup> For more detail, please see Debevoise Client Update, “FSA Consults on Changes to the Listing Regime, Focusing on Companies with Controlling Shareholders,” October 9, 2012.

shareholders will be required to comply, in full, at admission. For companies which already have a premium listing, the FCA is consulting on suitable “grace periods” for such companies to bring themselves into compliance.

## **INDEPENDENCE CRITERIA**

### *New Draft Rules*

The new draft rules enhance the current eligibility requirement that an applicant to the premium listing segment be carrying on an independent business as its main activity. They introduce a non-exhaustive list of factors indicating that the applicant is not capable of carrying on an independent business, including where the applicant lacks strategic control over the ability to earn revenue or the freedom to implement its business strategy, where most of the applicant’s revenue is attributable to transactions with a controlling shareholder, where the applicant cannot demonstrate that it has access to independent financing or where the applicant has been required to provide security over its business in connection with the funding of a controlling shareholder.

In addition, the new rules change the existing eligibility requirement that an applicant (other than a mineral company or scientific research company) control the majority of its assets, into one that is an additional factor which may indicate non-compliance with the overriding independent business requirement. For these purposes, an ability to exercise only negative control or to veto significant decisions affecting the management of the business would not be regarded as control. The new rules also introduce as an additional factor determining lack of independence the situation where the controlling shareholder appears to be able to influence the operations of the applicant outside its normal governance structures or through material shareholdings in one or more subsidiaries. Although deliberately broad in scope, the FCA has noted that this factor should not preclude the exercise of influence through normal governance structures such as representation on the board of directors.

## **AGREEMENTS WITH CONTROLLING SHAREHOLDERS**

### *New Draft Rules*

The FCA is re-introducing the concept of a “controlling shareholder” to mean a person who, together with its associates and parties “acting in concert” with it (as used in the context of the City Code on Takeovers and Mergers), owns 30% or more of shareholding or voting rights in a premium listed company. The new rules require that a company with a

controlling shareholder must enter into a shareholders agreement that includes the following three undertakings:

- Transactions and relationships between the company and the controlling shareholder or its associates will be conducted at arm's length and on normal commercial terms;
- No controlling shareholder or any of its associates will take any action that would have the effect of preventing the company from complying with its obligations under the Listing Rules; and
- No controlling shareholder or any of its associates will propose or procure the proposal of a shareholder resolution which is intended or appears to be intended to circumvent the proper application of the Listing Rules.

Although, as a matter of existing practice, many premium listed companies with controlling shareholders have such agreements in place, the agreements will still need to be reviewed to ensure that they include these three mandatory undertakings.

#### *Further Consultation*

The FCA is also consulting on further safeguards to encourage compliance with controlling shareholder agreements, including a requirement for the company to include in the annual report a statement as to whether the required agreement has been entered into with the controlling shareholder and the extent of compliance with the prescribed undertakings by both the controlling shareholder and the company, and including an explanation of any instances of non-compliance. If an independent director declines to support this statement, this must be disclosed and the FCA must be notified. In the event of a failure to conclude an agreement, non-compliance with the three prescribed undertakings or an independent director failing to support the compliance statement in the annual report, the FCA proposes that *all* transactions between the company and its controlling shareholder, including ordinary course of business and *de minimis* transactions, would be treated as if they were related party transactions and become subject to the prior approval of independent shareholders, until such time as the company's annual report includes a clean statement of compliance. If adopted, these rules could potentially lead to a significant increase in the responsibilities of independent directors in monitoring compliance with the terms of the controlling shareholder agreement.

## DUAL VOTING FOR THE ELECTION OF INDEPENDENT DIRECTORS

### *New Draft Rules*

The FCA is introducing a requirement for a dual voting procedure for the election and re-election of independent directors by companies with a controlling shareholder. This will require the separate approval of both a majority of all shareholders and a majority of independent shareholders. In the event that the two votes conflict, a further vote of all shareholders will be required at least 90 days after the first vote (in order to allow time for dialogue among the Company and the shareholders) and be decided on a simple majority basis. The proposals do not specifically extend to the removal of independent directors. These voting procedures will have to be incorporated into the company's constitution.

### *Further Consultation*

The FCA is also consulting on a requirement for companies with controlling shareholders (and potentially for all premium listed companies) to include detailed disclosure on the proposed independent directors in the circular sent to shareholders in advance of the AGM. Where a company already complies with the UK Corporate Governance Code, these proposals should not impose a significant additional burden as they are largely consistent with the responsibilities of the nomination committee of a premium listed company when selecting and recommending candidates for the board.

## CANCELLATION OF LISTING

### *Further Consultation*

Currently, in order to cancel a premium listing, or transfer to the standard listing segment, a premium listed company requires the prior approval of 75% of its shareholders. The FCA is consulting on whether to retain the current requirement or to require that, in addition, for a company with a controlling shareholder, the de-listing must be approved by a simple majority of the independent shareholders. The FCA is also consulting on corresponding amendments to the rules on cancellation of a premium listing in connection with a takeover offer by an offeror which is interested in more than 50% of the voting rights prior to the offer, to the effect that the offeror must obtain acceptances from a simple majority of independent shareholders. Exceptions are contemplated in certain situations in order to avoid excessively low free floats.

## OTHER CHANGES

### *New Draft Rules*

Other changes to the Listing Rules set out in the consultation paper include:

- a requirement that a premium listed company promptly notify the FCA of any instances of non-compliance with continuing obligations which are linked to the premium listing eligibility criteria;
- the introduction of two new Listing Principles for premium listed companies (that the voting power of each share within the same premium listed class should be equal and the voting rights of multiple classes of shares should not be disproportionate to the equity that they represent), as well as the extension of the application of two existing Listing Principles (in relation to adequacy of internal controls and dealing with the FCA in an open manner) to issuers with a standard listing;
- a requirement that a premium listed company's annual report present in readily identifiable form certain mandatory disclosures required under the Listing Rules;
- requirements in circumstances where a company has several classes of shares and not all classes are admitted to the premium listing segment to ensure that voting on matters which are prescribed by the Listing Rules as applicable to the premium listing segment will be decided by a resolution of holders of the shares admitted to the premium listing segment; and
- confirmation of the criteria that the FCA would follow in deciding whether to modify the 25% minimum free float requirement upon admission to the premium list (which include the number and nature of public shareholders and whether the expected market value of the free float shares exceeds US\$100 million) and clarification of the eligibility of certain holdings for inclusion in the free float (with shares subject to a lockup of more than 180 days non-eligible).

### *Further Consultation*

The FCA is also consulting on whether smaller related party transactions should be disclosed immediately rather than in the Company's annual report as at present.

## **NEXT STEPS**

Many of the new rules contained in CP 13/15 implement the key proposals introduced in CP 12/25 and are considered by the FCA as final as a policy matter, subject only to FCA Supervisory Board approval. The FCA is requesting feedback by February 5, 2014 on the additional consultation issues and then expects to introduce into effect the full package of revised rules by mid-2014.

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Please do not hesitate to contact us with any questions.

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