

Amendments to the Listing Rules

Relationship Agreements and appointing independent directors

May 2014

The FCA issued a consultation (Consultation Paper CP13/15) in November 2013 on amendments to the Listing Rules (the Rules). The FCA Board has now considered the amendments and changes to the Rules will come into force on 16 May 2014. One of the overriding themes of the amendments is the corporate governance standards to be applied to companies with a Premium Listing who have a Controlling Shareholder.

Controlling Shareholders

The majority of the new Rules will apply only to companies with a Premium Listing and which also have a "Controlling Shareholder". Part of the FCA consultation related to the definition of the term "Controlling Shareholder". The definition will now include any person who on his or her own, or together with any person with whom he or she is acting in concert, controls 30 per cent or more of the votes able to be cast on substantially all matters at a general meeting of a company. This definition is based on the substantial shareholder definition already contained in the related party transactions section of the Rules.

Relationship Agreements

As part of the changes, Premium Listed companies with a Controlling Shareholder will be required to enter into a "Relationship Agreement" with that shareholder. The minimum prescribed terms of the

Relationship Agreement must include undertakings that:

- transactions between the company and the Controlling Shareholder must be carried out on arm's length and normal commercial terms;
- the shareholder will not prevent the company from complying with the Rules; and
- the shareholder will not propose a resolution which, if passed, would cause the company to breach or seek to avoid the Rules.

Once the requirement for a Relationship Agreement has been incorporated into the Rules, companies with an existing Premium Listing and who have a Controlling Shareholder will have six months to put a Relationship Agreement in place. It is also proposed that Premium Listed companies in relation to which a person in the future becomes a Controlling Shareholder will have six months from the date the person becomes a Controlling

Shareholder to put in place a Relationship Agreement.

Relationship Agreements must stay in place for as long as the relevant person is a Controlling Shareholder.

Reporting requirements and non-compliance

A company with a Controlling Shareholder must include in its annual report:

- a statement that a Relationship Agreement has been entered into or, if not, that the FCA has been notified and the reason for the breach;
- a director's statement that the company and, as far as the company is aware, the Controlling Shareholder have complied with the terms of the Relationship Agreement, or, if they have not, a brief description of any breach(es) that have occurred; and
- a statement recording the fact that any independent director does not support the

declaration of compliance, if this is the case.

Non-compliance with the independence principles will lead to a company being subject to an enhanced oversight regime. This regime requires all transactions between a Controlling Shareholder and a company, irrespective of size, to be approved by the independent shareholders of that company (i.e. shareholders who are not the Controlling Shareholder or its associates).

Appointment of independent directors

Companies with a Premium Listing and a Controlling Shareholder will also be required to implement a dual-voting process for the appointment of independent directors. The appointment of each independent director will be subject to approval by two separate votes: one by the shareholders as a whole and a separate vote by the independent shareholders. If the two votes conflict, a second vote may be held at least 90 days but no more than 120 days after the original vote and may be passed on a simple majority basis. Any independent director whose appointment is the subject of a conflicting vote will serve as a director until the outcome of the second vote is known.

Once this amendment to the Rules is in force, companies with a Premium Listing and a Controlling Shareholder will be obliged to change their articles of association in order to provide for this dual-voting procedure. The FCA envisages that this required change to a company's articles will take place at the next general meeting (excluding a meeting for which notice has already been sent out) after the requirement comes into force.

Independent director disclosure requirements

A company adopting the dual-voting procedure will also be obliged to provide shareholders with information in relation to the independent director seeking appointment. This information includes:

- any past or existing relationships the director may have with the company or the Controlling Shareholder or a negative statement if no such relationships exist;
- any past or existing transactions the director may have entered into with the Controlling Shareholder;
- a statement by the company indicating why the company considers the director to be independent: in giving this statement the company will be expected to refer to the UK Corporate Governance Code; and
- a statement from the company as to why the company considers the director will be effective in the role to which he or she is being appointed.

The FCA is also consulting on whether these disclosure requirements should apply to all companies with a Premium Listing, rather than just those with a Controlling Shareholder.

Cancellation of listing

The changes in the Rules will also include a change to the delisting procedure for a Premium Listed company with a Controlling Shareholder. If such a company wishes to cancel its listing it must obtain the approval of 75 per cent of the shareholders of the company who vote on the resolution and a majority of the independent shareholders who vote on the resolution.

Corresponding requirements are to be introduced for a cancellation of a Premium Listing following a takeover. The procedure to be followed will differ depending on

the shareholding of the offeror before the announcement of a firm intention to make a takeover offer.

Where the offeror, or a Controlling Shareholder who is an offeror, is interested in 50 per cent or less of the company's voting rights the offeror will need to acquire or agree to acquire issued share capital representing 75 per cent of the voting rights in the company in order to cancel the company's listing.

However, where the offeror, or a Controlling Shareholder who is an offeror, is interested in more than 50 per cent of the company's voting rights the offeror must, in addition to reaching the 75 per cent threshold, obtain a majority of the votes held by independent shareholders. However, it should be noted that, if the offeror has agreed to acquire 80 per cent of the listed shares, then no approval by the independent shareholders is required.

Amendment to the free float level

The FCA also consulted on a proposed amendment to the minimum level of the free float on applications to the standard and premium segments. Under current Rules, 25 per cent of a class of securities for which application for admission has been made are in public hands, although the FCA has the power to lower this percentage at its discretion in individual cases.

After considering the results of the consultation the FCA has decided not to make any adjustment to the free float level. The FCA stated that modifying the level of the free float in order to improve minority shareholder participation in corporate governance was, in its view, disproportionate. The FCA is satisfied that the proposed provisions on the appointment of independent directors and Relationship Agreements will

sufficiently enhance protection for minority shareholders, thus achieving the FCA's aims in a more proportionate manner. In rejecting this proposed amendment to the Rules the FCA did make a number of other statements of clarification, including:

- when considering whether to exercise its discretion to allow

a reduced free float level, the FCA stated that, the larger the level of the reduction (below 25 per cent), the "weightier" the evidence on future liquidity would need to be in order for its discretion to be exercised; and

- where such a modification to the free float level is agreed to, the FCA will continue to monitor the liquidity of the

securities. The FCA has introduced new guidance to this effect, which also clarifies the steps it may take if the expected liquidity does not materialise. These include the withdrawal of the agreed reduction to the free float level.

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