

## News round-up

### Corporate finance

#### Introduction

Welcome to the latest in our series of regular alerts containing a round-up of news from our capital markets practice. Corporate governance is again in the news and we report on this and other developments below.

#### **Company law: European company law: European Commission launches consultation on the future of European company law**

On 20 February 2012, the European Commission launched a consultation on the future of European company law. Its aim is to find out whether the existing framework meets current needs and where improvements could be made. The issues addressed are wide-ranging and include:

- the objectives and scope of European company law;
- whether there should be further regulation of the cross-border mobility of companies; and
- whether there is a need to review the capital regime for European companies.

The consultation closes on 14 May 2012. The Commission will issue a feedback statement in mid-2012 and announce any follow-up initiatives in the second half of the year.

European Consultation: Consultation on the future of European Company Law available at:

<http://ec.europa.eu/yourvoice/ipm/forms/dispatch?form=companylaw2012>

#### **Company law: the UK Government seeks comments on stream-lining company law**

In the meantime, the UK Government has been seeking comments on various aspects of company law with the aim of reducing the burden of regulation on UK businesses. This initiative forms part of the Government's so-called 'Red Tape Challenge'. The consultation closed on 16 February 2012 and the results will be published later in the year.

Red Tape Challenge: Department for Business, Innovation and Skills Discussion paper: 'Providing a flexible framework which allows companies to compete and grow' available at:

<http://www.bis.gov.uk/assets/biscore/business-law/docs/c/12-560-company-law-flexible-framework-discussion-paper.pdf>

#### **Corporate governance: the FRC publishes report with advice on the content of an 'explanation' under the 'comply or explain' regime of the UK Corporate Governance Code**

On 15 February 2012, the Financial Reporting Council ('FRC') published a report which aims to clarify what will constitute an 'explanation' under the 'comply or explain' regime of the UK Corporate Governance Code ('the Code'). The report, which reflects the FRC's aim of reinforcing its approach, follows discussions between the FRC and senior company and investor representatives. It advises that the key elements of an explanation should include

- a description of the background;
- a clear rationale specific to the company;
- an indication whether the company's deviation from the Code is limited in duration; and
- an indication of the alternative measures the company is taking to comply with the Code and to mitigate any additional risk.

Members of the discussion group also consider that there should be an improvement in the quality of disclosure generally and that each company should make clear how its governance arrangements support its business model.

The FRC has yet to decide whether it will take the findings of its discussions into account in the revisions to the Code on which it will be consulting later in the year.

FRC Report: What constitutes an explanation under 'comply or explain'? Report of discussions between companies and investors available at:

<http://www.frc.org.uk/images/uploaded/documents/FRC%20explanations%20paper%200301121.pdf>

### **Corporate governance: PIRC publishes its 2012 UK shareholder voting guidelines**

The Pensions Investment Research Consultants ('PIRC') has published the latest edition (the 16th) of its UK Shareholder Voting Guidelines, aimed at institutional investors, to replace the version published in March 2011. The latest edition of the guidelines reflects the general concern of PIRC that a number of corporate decisions have been based on company values that do not meet legal obligations. Among other things, it also addresses two other areas of concern to PIRC:

- the preservation and stewardship of capital: the revised guidelines stress the importance of the audit and the accounts in protecting capital and dividend legitimacy; and
- share buy-backs: PIRC is, for the moment, reserving its position on voting recommendations amid concerns that boards may not always have all relevant information when they make decisions to buy back shares that are perceived to be undervalued.

PIRC 2012 UK shareholder voting guidelines available to order from the PIRC web-site: <http://www.pirc.co.uk/>

### **Corporate governance: the QCA publishes remuneration committee guide for smaller quoted companies**

The Quoted Companies Alliance ('QCA')<sup>1</sup> has published (5 March 2012) its Remuneration Committee Guide for Smaller Quoted Companies containing best practice guidelines with the aim of providing practical guidance on developing a bespoke, appropriate approach to remuneration. The guide discusses the objectives of the remuneration committee, the factors it should consider in setting remuneration policy, the question of communicating with shareholders, and the membership, organisation and functions of the committee.

QCA Remuneration Committee Guide for Smaller Quoted Companies available to order from the QCA web-site: <http://www.theqca.com/shop/guides/>

### **Corporate governance: women on boards: EU initiative**

The European Commission has launched a consultation (on 5 March 2012) regarding possible EU action to deal with the current gender imbalance on corporate boards within the EU. The Commission is concerned that little progress has been made in this area. The Commission is seeking comments on a number of issues, including the following:

- which types of companies should be covered by the initiative and whether it should apply to all categories of directors (executive and non-executive);
- the percentage of available board positions that women should occupy; and
- the effectiveness of self-regulation and whether additional forms of action should be taken.

<sup>1</sup>: The QCA represents small and mid-cap companies outside the FTSE 350, including those on AIM and PLUS Markets.

Comments are requested by 28 May 2012. The Commission will decide what further action to take (and this may include legislation) later in the year.

In the meantime, the UK Government continues to encourage companies to deal with this issue by voluntary means.

European Commission: consultation on gender imbalance in corporate boards in the EU available at:

[http://ec.europa.eu/justice/newsroom/gender-equality/opinion/files/120528/28051\\_consultation\\_questions\\_en.doc](http://ec.europa.eu/justice/newsroom/gender-equality/opinion/files/120528/28051_consultation_questions_en.doc)

### **Corporate performance: UK equity markets and long-term decision making: the Kay Review publishes an interim report**

Professor Kay issued his interim report into the UK equity markets and long-term decision making by UK companies on 29 February 2012. This forms part of the Government's consultation, 'A Long-Term Focus for Corporate Britain', launched in October 2010, to consider ways directors, shareholders and investors can work in the long-term interests of the UK economy and UK businesses.

Professor Kay's independent review focuses on the incentives, motivations and time-scales of participants in UK equity markets, and the effect these have on the corporate decision making and long-term performance of UK companies, rather than on the corporate governance aspects of the consultation.

Professor Kay's interim report refers to the issues raised by respondents in response to his call for evidence issued in October last year (which include matters relating to the company and the board, asset managers and intermediaries) and seeks further evidence concerning these points. No recommendations have been made at this stage.

Comments are requested by 27 April 2012. Professor Kay's final report (with his recommendations) is due to be submitted to the Government this summer.

The Kay Review of UK Equity Markets and Long-Term Decision Making: Interim Report available at:

<http://www.bis.gov.uk/assets/biscore/business-law/docs/k/12-631-kay-review-of-equity-markets-interim-report>

### **Financial reporting standards: the ASB proposes to replace existing UK accounting standards with a single financial reporting standard**

On 30 January 2012, the Accounting Standards Board ('ASB') published for consultation revised proposals for the future of financial reporting standards in the UK and Republic of Ireland. Its principal recommendation is that all current UK accounting standards should be replaced by a single financial reporting standard based on the International Financial Reporting Standards for small and medium-sized enterprises (which would lead to a reduction in the volume of accounting standards). The ASB has also published the alternative view of one member of the ASB who disagrees with the proposed approach.

The ASB invites comments by 30 April 2012 and proposes that the changes will be effective for accounting periods beginning on or after 1 January 2015.

Revised Financial Reporting Exposure Draft: The Future of Financial Reporting: Part One; Explanation available at:

<http://www.frc.org.uk/images/uploaded/documents/Part%201%20Web%20Optimized%20Feb%209th%202012.pdf>

Revised Financial Reporting Exposure Drafts 46, 47 and 48: The Future of Financial Reporting: Part Two: The Drafts Standards available at:

<http://frc.org.uk/images/uploaded/documents/Part%202%20Web%20Optimized1.pdf>

Revised Financial Reporting Exposure: The Future of Financial Reporting: Part Three: Development of the Financial Reporting Exposure Drafts and Impact Assessment available at:

<http://frc.org.uk/images/uploaded/documents/Part%203%20Web%20Optimized1.pdf>

Alternative view available at: Revised FRED: The Future of Financial Reporting – Alternative View:

<http://frc.org.uk/images/uploaded/documents/Alternative%20View%203rd%20Proof.pdf>

### **Listing Rules: the FSA consults on changes to the Listing Rules**

On 26 January 2012, the Financial Services Authority ('FSA') issued a consultation paper (CP12/2) setting out proposals for changes to the Listing Rules ('LR') to update the LR to reflect recent changes in market practice. The proposed changes include the following:

- the reverse takeover regime (LR5): at present, the acquisition of one listed company by another is not a reverse takeover. In order to ensure that reverse takeovers cannot be used as a "back-door" route to listing, the current exemption will be limited so that only acquisitions by a listed company of a listed company in the same listing category (i.e. premium or standard) will be exempt from the reverse takeover regime; and
- the sponsors regime (LR 8): the proposals reflect the FSA's aim to increase the role and responsibility of sponsors and would, for example, allow the FSA to require sponsors to provide the FSA with such information as it reasonably requires to ensure that the LR are being complied with by an issuer.

The FSA also refers to the quality of the premium listing standard in light of the changes made recently by FTSE to the UK Index Series Ground Rules, together with the general focus on corporate governance, and invites comments on whether any changes are needed to the LR to give additional protection to investors.

Comments are requested by 26 April 2012.

Consultation Paper CP12/2: Amendments to the Listing Rules, Prospectus Rules, Disclosure Rules and Transparency Rules available at: <http://www.fsa.gov.uk/library/policy/cp/2012/12-02.shtml>

### **Market abuse: the FSA considers the "reasonable investor" defence in £7.2m Einhorn enforcement action**

On 12 January 2012, the Financial Services Authority ('FSA') fined David Einhorn, the owner of the US hedge fund Greenlight Capital Inc. ('Greenlight'), and his fund £7.2 million for engaging in the market abuse offence of insider dealing under s. 118 of the Financial Services and Markets Act 2000 ('FSMA') in connection with an anticipated equity fundraising by Punch Taverns Plc ('Punch') in June 2009. The FSA made this finding even though David Einhorn and Greenlight had received the relevant information on the explicit understanding that they were not being made insiders.

On 9 June 2009, David Einhorn had taken part in a telephone conference in which a corporate broker acting, on behalf of Punch, disclosed that Punch was at an advanced stage of the process towards a significant equity fundraising. Some minutes after the telephone call, David Einhorn gave instructions for the sale of all Greenlight's holdings in Punch. At the time of the instructions, Greenlight held 13.3% of Punch's issued equity and over the next four days reduced its holding to 8.89%.

Some six days after the telephone conference, Punch announced a rights issue to the market and its shares subsequently fell by 29.9%. Greenlight's trading prior to the announcement meant that it had avoided losses of approximately £5.8 million in respect of the funds under its management.

David Einhorn (and Greenlight) had, prior to the telephone conference, specifically asked not to be wall-crossed (that is, not to receive inside information) and David Einhorn did not believe that the information he had received during the telephone call constituted inside information.

An important aspect of the case relates to the FSA's approach to the 'reasonable investor' defence to market abuse contained in s. 123(2) FSMA (on which David Einhorn had sought, in part, to rely).<sup>2</sup>

The FSA accepted that David Einhorn's trading was not deliberate because he did not believe that it was inside information. However, the FSA did not consider that this was a reasonable belief. In its view, David Einhorn should have been aware that he had inside information (or that there was a risk of this) and that he was responsible for considering whether the information was, in fact, inside information notwithstanding his request not to be wall-crossed.

<sup>2</sup>: Section 123(2) FSMA provides that the FSA may not impose a penalty if there are reasonable grounds for it to be satisfied that (1) the person believed, on reasonable grounds, that his behaviour did not fall within the market abuse regime and (2) the person took all reasonable precautions and exercised all due diligence to avoid breaching that regime.

The FSA fined David Einhorn the sum of £3,638,000, including disgorgement of financial benefit, and fined Greenlight the sum of £3,650,795 (again, including disgorgement of financial benefit).

The FSA has also fined the broker who disclosed the information regarding Punch's proposed equity issue during the course of the telephone conference of 9 June 2009 for engaging in the market abuse offence of improper disclosure of inside information in breach of section 118(3) of FSMA.

FSA decision notice: David Einhorn available at: <http://www.fsa.gov.uk/static/pubs/decisions/dn-einhorn-greenlight.pdf>

FSA decision notice: Greenlight Capital Inc. available at: <http://www.fsa.gov.uk/static/pubs/decisions/dn-greenlight-capital.pdf>

### How Squire Sanders can help

We would be pleased to discuss with you in more detail any of the matters raised in this article.

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