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UK PUBLIC COMPANY /AIM MARKET

AIM Rule Amendments relating to Subscription Periods

On 10 February 2009, the London Stock Exchange announced that in response to FSA Consultation Paper CP09/04 on rights issue subscription periods, changes were being made to the AIM Rules for Companies to reflect the FSA's decision to reduce the minimum rights issue subscription period to 10 business days. The required changes are to the note to AIM Rules 24 and 25 and they are of immediate effect.

New ABI Guidance: Limits for General Authority to Allot Shares

The Association of British Insurers ("ABI") has issued replacement guidance for companies seeking general authority from shareholders to allot shares, which it will review after three years in operation. Under the new guidance, the overall allotment headroom in respect of which authority may be sought under section 80 of the Companies Act 1985 will be increased, so that in addition to the usual authority to allot up to the lesser of the unissued ordinary share capital and one third of the issued share capital, companies will be able to seek authority to allot equity securities up to a further one third of their issued share capital, subject to certain limitations.

The additional headroom will only be available for fully pre-emptive rights issues (and not open offers or other types of pre-emptive offerings) and the authorisation should only be valid for a year rather than up to the five years permitted by the ABI in relation to the usual one third authority. It also appears, although the drafting of the ABI guidance is not clear, that all board members wishing to remain in office will be expected to stand for re-election at the annual general meeting immediately following any decision to allot new shares under the additional authority which results (i) in the number of shares issued exceeding one third of the nominal amount of the issued share capital; and (ii) the issue proceeds exceeding one third (or such relevant lesser proportion) of the pre-issue market capitalisation of the company.

Companies are expected to continue to comply with the Pre-Emption Group's Statement of Principles with regard to annual and cumulative limits for routine disapplications of the statutory pre-emption rights. In line with its recent practice, the ABI has now stated that companies will be expected to confirm, at the time any disapplication of statutory pre-emption rights is sought, their intention to comply with the principle that, in any rolling three year period, non pre-emptive issues of shares will not exceed 7.5% of a company's issued share capital.

Cash Box Placings: ABI concern

In a letter to directors of listed companies, the ABI has raised concerns that the recent resurgence of the cash box placing as a means of capital raising by companies could lead to an erosion of the pre-emption principle. A cash box placing enables a company to issue shares without the need to use its annual statutory pre-emption disapplication as the new shares are issued in consideration for the acquisition of shares, not cash. Cash box placings therefore circumvent the annual limit imposed on listed companies by the Pre Emption Group Guidelines, which restricts new issues of shares for cash to 5 per cent. of the issued share capital.

In a typical cash box structure, a new company, "Newco", is incorporated by the issuer (usually in Jersey). The issuer's financial adviser then undertakes to subscribe for redeemable preference shares in Newco at a value equal to the proceeds of the placing shares to be issued by the Company (less commissions and expenses) conditional upon admission of the placing shares. At the same time, the Issuer issues the placing shares to placees, in consideration for the agreement by the financial adviser to transfer the Newco redeemable preference shares and ordinary shares held by it to the Issuer. The net placing proceeds are applied by the financial adviser for the subscription of the Newco redeemable preference shares.

A cash box placing therefore provides a company with a more efficient means of raising funds from a share issue that avoids having to increase any existing disapplication authority and therefore transactional delay that otherwise results when shareholder approval is required. However, companies listed on the Official List would need to issue a prospectus if during any twelve month period shares in excess of 10 per cent. of the issued share capital are issued. Another advantage of the cash box structure is that it may enable a company to create distributable reserves, by taking advantage of the merger relief provisions in section 131 Companies Act 1985 which in certain circumstances allow it to treat the premium over nominal value at which shares are issued as realised profit.

There has been considerable debate as to whether a cash box structure is merely a device for avoiding the statutory pre-emption protections although the prevailing view appears to be that such transactions should instead be characterised as making use of a series of legal steps that bring them within the exceptions provided by statute. Whatever the legal justification for cash-box placings however, it is clear that they are not welcomed by institutional shareholders and issuers will need to bear their views in mind when considering raising additional capital.

Amendment to DTR's: Disclosure of CfDs

The FSA has published Policy Statement 09/3 giving feedback on the consultation process relating to the introduction of disclosure obligations in respect of interests in contracts for difference and other similar instruments and setting out the revisions to the Disclosure and Transparency Rules, which will now take effect from 1 June 2009, three months earlier than originally intended.

The new provisions relate to interests in financial instruments that are referenced in whole or in part to the shares of a UK incorporated issuer listed on a regulated or prescribed market. From 1 June 2009, direct or indirect interests held by a person in qualifying financial instruments and instruments having an equivalent effect and which relate to the same UK issuer will need to be aggregated and notified where the applicable thresholds are reached, that is, three per cent. and at one per cent. increments thereafter. Exemptions will apply to client-serving intermediaries satisfying certain criteria.

The FSA considers that a financial instrument will have a similar economic effect to a qualifying financial instrument if its terms are referenced in whole or in part to an issuer's shares and, generally the holder of the financial instrument has, in effect, a long position on the economic performance of the shares whether the instrument is settled physically or in cash. The FSA has confirmed that in its view convertibles or other instruments relating to shares not yet in issue would be within the scope of the new disclosure regime.

Financial instruments that do not have a delta 1 profile (*i.e* where the value of such instruments does not have a one to one relationship with the value of the underlying shares), for example, cash settled derivatives, will need to be disclosed on a delta-adjusted basis rather than a nominal basis. However, during the period 1 June to 31 December 2009, transitional provisions will permit the reporting of positions on either a delta-adjusted or nominal basis, provided that in the latter case the strike or exercise price and the total number of voting rights relating to each financial instrument is also reported.

Financial instruments referenced to a basket of shares or an index will not be disclosable unless the shares in the basket represent 1 per cent. or more of the class in issue and 20 per cent. or more of the value of the securities in the basket or index and the use of the financial instrument is connected to the avoidance of notification.

The new disclosure requirements will apply alongside the disclosure requirements under the City Code on Takeovers and Mergers during an offer period, entailing separate disclosures for each regime.

PROSPECTUS DIRECTIVE

Review of Prospectus Directive

The European Commission has published a consultation document containing proposals which aim to simplify and improve the implementation of the Prospectus Directive (2003/71/EC) in the EU and reduce the administrative burden on issuers.

The proposed changes include:

- amending the definition of "qualified investor" to include "professional clients" under MiFID;
- extending the exemption for employee share schemes so that it applies to third country issuers listed on a third country exchange but not listed on a regulated market, non-listed companies and companies listed on exchange regulated markets, for example AIM;
- deletion of the requirement for a company to produce an annual information document; and
- harmonising the period during which withdrawal rights may be exercised following publication of a supplementary prospectus.

The document also seeks comment on further issues including whether to abandon the requirement for a prospectus in relation to a rights issue (subject to publication of a circular) and the information to be included in a prospectus where debt issues are guaranteed by member states.

CESR Publication of Revised Frequently Asked Questions relating to Prospectuses

On 10 February 2009, the Committee of European Securities Regulators ("CESR") published the eighth version of the set of frequently asked questions regarding prospectuses: common positions agreed by CESR members. This includes a new question regarding employee share scheme prospectuses and the short form disclosure regime for offers to employees in those cases where a prospectus is required.

Currently, the only exemption for employee share schemes in the Prospectus Directive relates to those companies whose securities are listed on a Regulated Market within the European Economic Area ("EEA"). This means that there is no exemption for:

- Companies whose securities are traded on any other market within the EEA (*e.g.* AIM).
- Companies whose securities are traded on investment exchanges outside the EEA.
- Private and unquoted public companies.

In December 2007 CESR stated it intended to analyse the possibility of agreeing a short form disclosure regime for employee share scheme prospectuses. CESR has now concluded that a full prospectus is not an effective way of informing employees about the risks and benefits of an offer of securities whilst also imposing excessive cost on employers.

So until such time as the European Commission amends the Prospectus Directive in respect of offers to employees where a prospectus is required, CESR has set out a short form disclosure regime for offers to employees to be adopted in such cases. Further, CESR intends that companies with shares listed or admitted to trading on AIM or non-EEA markets should be able to take advantage of the new approach. However, private and unquoted public companies will still need to consider whether a full prospectus might be required for any employee offer.

It remains the case, however, that the competent authority will need to scrutinise and approve a prospectus following the short form disclosure regime.

TAKEOVERS AND MERGERS

Extension of City Code to Isle of Man Companies

From 1 March 2009, the City Code now applies to Isle of Man companies with appropriate modifications.

UK COMPANY LAW

Proper Purpose Test and Access to Register of Members

Following the implementation of Part 8 of the Companies Act 2006, access to a company's register of members is subject to a proper purpose test. Under section 116 Companies Act 2006 a request for a copy of a company's register of members must include the name and address of the applicant, the purpose for which the information will be used, whether the information will be disclosed to any other person and, if so, the equivalent information for that person. A company may apply to the court for a declaration under section 117 if it is uncertain whether the information will be used for a "proper purpose", although this term is not defined.

The Institute of Chartered Secretaries and Administrators has published an updated guidance note which includes advice as to what may or may not constitute a "proper purpose", recommendations as to best practice for dealing with section 116 requests and a brief overview of the applicable court procedures.

Protection of Directors' Residential Addresses

From 1 October 2009 under the Companies Act 2006, directors' residential addresses will become protected information and limits on disclosure of this information will apply to both the company and the Registrar of Companies. A director will still be obliged to provide his residential address to the Registrar together with a service address but only the service address will appear on the public record. Companies may only use a director's residential address to communicate with the director or to comply with its obligations to provide this information to the Registrar. The Registrar will be unable to use or otherwise disclose the information except to a permitted public authority or credit reference agency under certain conditions. In some circumstances, individuals, who are able to demonstrate that, for example, disclosure of such information could endanger them, will be able to apply to the Registrar requesting that it refrain from disclosing the information to credit reference agencies. To the extent that a director's service address and residential address are the same, this fact will constitute protected information, although the service address will continue to be publicly available.

UK COMPANY TAX

Corporation Tax Act 2009

On 1 April 2009, the Corporation Tax Act 2009 came into force. The Act applies to accounting periods of UK taxable companies ending on or after 1 April 2009, and forms part of HM Revenue and Custom's ongoing Tax Law Rewrite project. As such, it is the first of two statutes rewriting the main body of the UK corporation tax regime in order to simplify the UK corporation tax legislation, broadly, without changing the substance of the existing tax law (eventually replacing the Income and Corporation Taxes Act 1988 as well as other applicable statutes). The second new corporation tax statute is expected to come into effect in 2010.

CORPORATE GOVERNANCE

GMG First Report on Transparency and Disclosure in Private Equity

On 12 January 2009, the Guidelines Monitoring Group ("GMG") established by the British Venture Capital Association ("BVCA"), published its first report on compliance by the private equity industry with the Walker Guidelines ("Guidelines") on disclosure and transparency in private equity. The Guidelines, originally published in November 2007, are intended to form the basis of a voluntary system of disclosure which promotes conformity with established best practice in the private equity industry. To date, 32 private equity firms and 54 of their portfolio companies have signed up to the Guidelines.

The Guidelines include enhanced disclosure requirements for portfolio companies where they have more than 1,000 UK employees, generate more than 50% of their revenues in the UK and either have an enterprise value of more than £500 million when acquired by the private equity buyer or, in the case of a public to private transaction, had a market capitalisation together with a premium for control of more than £300 million. The enhanced requirements include a recommendation to include in the annual financial review, information on risk management objectives and policies in light of the principal financial risks and uncertainties facing the company and as part of the annual report, a business review substantially conforming to the provisions of section 417 of the Companies Act 2006, including the enhanced business review requirements that are ordinarily applicable to listed companies.

The GMG considers that in the first year since introduction of the Guidelines, there has been a high level of support shown by the private equity industry. The GMG found that a "substantial majority" of the firms and portfolio companies reviewed had made good or acceptable disclosures, with only a limited number of exceptions. However, the nature of disclosure currently "varies significantly", particularly in relation to portfolio companies' compliance with the requirements of the "enhanced business review" of section 417 of the Companies Act 2006 (although in this, portfolio companies were being asked to comply 12 months before listed companies are required to do so, meaning that there was no existing best practice on which to base such a review).

Overall, only a small number of portfolio companies reviewed did not meet the Guidelines' enhanced disclosure requirements to a satisfactory degree. The GMG has written to the private equity owners of these companies to request specific confirmation of the actions to be taken to address the exceptions and has since received commitments to take corrective action in respect of each of the companies concerned.

The GMG found that the private equity firms reviewed met the other requirements and recommendations of the Guidelines without exception.

QCA Audit Committee Guide

In February 2009, the Quoted Companies Alliance ("QCA") published its Audit Committee Guide for Smaller Quoted Companies ("Guide") in order to help audit committee members and their chairmen to manage audit committee business efficiently and to report effectively on performance to investors. The Guide covers:

- Audit committee membership and organisation.
- Oversight of the annual accounts cycle.
- External auditors.
- Risk management and internal controls.

Revisions to NAPF Corporate Governance Policy and Voting Guidelines

On 6 February 2009, the National Association of Pension Funds ("NAPF") announced revisions to its Corporate Governance Policy and Voting Guidelines for 2008/2009. Although there has been no change to remuneration policy, the general observation is that in light of the present crisis it is likely that investors will take a less tolerant view of non-compliance with the Combined Code for which the explanation of non-compliance is deemed unsatisfactory.

In relation to specific resolutions to be proposed by companies, the NAPF considers that a resolution to remove a borrowing limit altogether from the articles of association of a company would be unacceptable (in all but exceptional circumstances) and that if increasing the existing limit in the articles, companies should specify a new limit.

In reaffirming its support of company pre-emption rights on new share issues, the NAPF has voiced concern about the increasing use of cash boxes to circumvent existing cash allotment authority limits. Also, the NAPF is proposing that the existing 5% limit on the authority to allot shares for cash be increased to 10% for companies on AIM.

CONTRACT/COMMERCIAL

Rome II Regulation on the Law Applicable to Non-Contractual Obligations

The Rome II Regulation on the Law Applicable to Non-Contractual Obligations (*864/2007/EC*) ("Rome II") has come into force with effect from 11 January 2009. It requires the courts of all EU member states (other than Denmark) to apply the same set of rules in determining the law that governs non-contractual obligations in the majority of civil and commercial matters. Once the applicable law is ascertained under Rome II, that law will govern not only the basis and extent of a party's liability, but such matters as the grounds for exemption from, and limitation of, liability and, significantly, the existence, nature and assessment of damages.

The general rule under Rome II is that the law applicable to non-contractual obligations is the law of the country in which the damage occurs. There are, however, exceptions to which the general rule does not apply, *e.g.* where the party liable and the party suffering damage both have their habitual residence in the same country or where the relevant tort is manifestly more closely connected with another country.

The introduction of Rome II provides greater certainty as to the law which will apply to a tort in the EU. In certain cases it will be possible to choose the law that will apply. However, it is difficult to predict all the circumstances that might give rise to a claim and there is a risk that the chosen law might turn out to be less favourable than the law which would otherwise have applied.

Mercury Tax Case: Revisiting execution and completion practice

The debate continues over the implications of certain obiter remarks made as part of the decision in the case of *R (on the application of Mercury Tax Group Limited and others) v HMRC and others [2008] EWHC 2721 (Admin) 2008*. In this case it was held that a deed was not properly executed and effective where an earlier version was executed but the signature page was "recycled" and subsequently appended to a later draft. Although the facts of the case centred around the validity of a deed, the court's comments encompassed both contracts by way of deed and simple contracts. The case has generated significant concern as to the process for completing transactions where not all parties are physically present for signing. The Law Society Company Law Committee and the City of London Law Society Company Law and Financial Law Sub-Committees are currently in the process of drafting (non-binding) guidance on execution and completion practices to assist practitioners in this area.

EMPLOYMENT

Abolition of statutory disciplinary and grievance procedures

From 6 April 2009 the statutory disciplinary and grievance procedures in force since 2004 will (subject to transitional provisions) be replaced by a simpler system. The existing procedures have proved to be unduly onerous in practice, as any failure to observe the procedure has resulted in "automatic unfair dismissal" even for non-substantive failures. If the failure was "flagrant" this could lead to an uplift in an award by the Employment Tribunal of up to 50%. Tribunals will now compare how employers behave in contrast to the non-statutory code adopted by ACAS (the Advisory, Conciliation and Arbitration Service) and although a failure to comply will make a finding of unfair dismissal more likely, it will not be automatic. In addition, failures by employers may lead to uplifts in awards of up to 25% and failures by employees, to reductions in awards of up to 25%. The new code will not apply to redundancy dismissals or non-renewal of fixed-term contracts. Unlike the statutory code, the new code does not require grievances to be raised in writing or be a prerequisite to starting proceedings in the Employment Tribunal.

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