SHEARMAN & STERLING LLP

A QUARTERLY NEWSLETTER FOR CORPORATES

JULY 2014/EUROPE

Governance & Securities Law Focus

In this newsletter, we provide a snapshot of the principal European, US and selected international governance and securities law developments of interest to European corporates.

The previous quarter's Governance & Securities Law Focus newsletter is available here.

Financial regulation developments are available here.

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EU DEVELOPMENTS

Statutory Audit Directive and Regulation Published in Official Journal

On 27 May 2014, the directive amending the Statutory Audit Directive and a new regulation regarding the statutory audit of public interest entities were published in the Official Journal. The legislation will come into force 20 days later. The regulation will apply in member states from 17 June 2016, other than the prohibition on "Big Four only" contractual clauses (Article 16(6)), which will apply from 17 June 2017. Member states will be required to adopt the necessary measures to implement the directive by 17 June 2016.

The legislation is aimed at addressing the weaknesses highlighted in the European audit system following the 2008 financial crisis. Key elements of the regulation include:

- prohibition on contingent fees and a 70% cap on fees for non-audit services;
- prohibition of the provision of non-audit services;
- increased disclosure requirements for the auditor's report (including who appointed the audit firm, the date of appointment and period of total uninterrupted engagement, including previous renewals and reappointments of the statutory auditors or the audit firms); and
- prohibition on "Big Four only" contractual clauses regarding the appointment of statutory auditors or audit firms.

Key elements of the directive include:

- amended provisions on the auditor's independence and objectivity and organisation of the auditor and the audit work;
- clarification of the scope of the statutory audit; and
- a European passporting regime to enable auditors to exercise their profession across Europe.

The legislation is available at:

http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:L:2014:158:FULL&from=EN

Council Adopts Intra-Corporate Transferees Directive

On 13 May 2014, the General Affairs Council formally adopted the proposed directive of the European Parliament and of the Council on conditions of entry and residence of non-EEA nationals in the framework of an intra-corporate transfer. The directive will now be published in the Official Journal and member states will have to transpose it within two and a half years of its publication.

The directive is aimed at making it easier and quicker for multinational companies to temporarily assign highly skilled non-EEA employees to subsidiaries situated in the EU, to facilitate mobility of intra-corporate transferees between member states during their assignments, and to avoid exploitation and distortion of competition by laying down a common set of rights for such intra-corporate transferees when working in the EU. According to the Commission, 15,000 to 20,000 non-EEA national intra-corporate transferees will be admitted annually in the framework of this directive.

This directive is part of the EU's new common policy on legal migration and complements three existing legal migration directives setting out the admission criteria for and the rights of highly qualified third-country workers.

The proposed directive is available at:

http://register.consilium.europa.eu/doc/srv?l=EN&f=PE%2058%202014%20INIT

ESMA Publishes Consultation and Discussion Paper on MiFID II

On 22 May 2014, the European Securities and Markets Authority ("ESMA") published a consultation and discussion paper regarding the draft technical advice on the content of the delegated acts required by the revised Markets in Financial Instruments Directive (the "MiFID II") and the Markets in Financial Instruments Regulation ("MiFIR") it is required to provide to the European Commission.

ESMA is advising the European Commission on MiFID II implementing measures with regard to the organisational requirements and operating conditions for investment firms. These include the areas of:

- investor protection;
- transparency;
- data publication;
- microstructural issues;
- requirements applying on and to trading venues;
- commodity derivatives; and
- portfolio compression.

Under MiFID I these implementing measures were contained in the MiFID Implementing Directive. ESMA considers that several existing requirements of the Implementing Directive are in line with the MiFID II framework, and so do not need to be replaced. The consultation and discussion papers instead focus on areas in which new requirements or modifications to the Implementing Directive are proposed.

ESMA must conduct a public consultation before submitting draft regulatory technical standards ("RTS") and implementing technical standards to the European Commission.

ESMA will therefore consider the responses it receives to the consultation paper and will finalise the draft technical advice for submission to the European Commission by no later than six months after the entry into force of MiFID II and MiFIR.

The consultation paper is available at:

http://www.esma.europa.eu/system/files/2014-549_-_consultation_paper_mifid_ii_-_mifir.pdf

The discussion paper is available at:

http://www.esma.europa.eu/system/files/2014-548_discussion_paper_mifid-mifir.pdf

Omnibus II Directive Published in the Official Journal

On 22 May 2014, the Omnibus II Directive which, among other things, will amend the Prospectus Directive in respect of the powers of ESMA, was published in the Official Journal.

The Prospectus Directive will be amended to require the competent authority of the relevant home member state of the issuer to communicate final terms of any offer that are neither included in the base prospectus nor in a supplement to the

competent authority of the host member state and to ESMA (in place of communication by the issuer, offeror or person asking for admission to trading on a regulated market). The directive also sets out ESMA's obligation to draft RTS for the European Commission in respect of:

- the information that may be incorporated by reference in a prospectus;
- the procedures for the approval of the prospectus and the conditions in accordance with which time limits for approval may be adjusted;
- the provisions relating to the publication of the prospectus; and
- the provisions concerning the dissemination of advertisements announcing the intention to offer securities to the public or admission to trading on a regulated market.

The directive entered into force on 23 May 2014 and must be transposed into national law and regulation by 31 March 2015 and applied from 1 January 2016.

The directive is available at:

http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=uriserv:OJ.L_.2014.153.01.0001.01.ENG

Publication of Prospectuses in Electronic Form

A recent case of the European Court of Justice (*Michael Timmel v Aviso Zeta AG* (Case C-359/12)) considered whether the requirement in Article 29 of the Prospectus Regulation for a prospectus published in electronic form to be easily accessible was met when the relevant prospectus was published on a website which required certain conditions to be met before access was allowed.

The ECJ ruled that the requirement in Article 29 is not met where the prospectus is published on a website that requires the acceptance of a disclaimer and the obligation to register on that website, the obligation to provide an email address or where a charge is made for access to that website, or where consultation of parts of the prospectus is restricted to two documents per month.

The judgment is available at:

http://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1395663271645&uri=CELEX:62012CJ0359

Shareholder Rights Directive – European Commission Proposal for Amending Directive

On 9 April 2014, the European Commission published a proposal to amend the Shareholder Rights Directive.

The proposal includes provisions under which, briefly:

- companies must disclose their remuneration policy and the individual remuneration of directors. Shareholders will have the right to approve the remuneration policy and vote on the remuneration report and, subject to a limited exception in case of new board members, companies may only remunerate directors in accordance with the policy approved by shareholders;
- related party transactions (defined by reference to international accounting standards) representing more than 5% of company assets, or transactions which could have a significant impact on profits or turnover, will be subject to shareholder approval. Smaller related party transactions representing more than 1% of assets must be publicly announced at the time of conclusion, with the publication of an independent third party report. Member states may exclude transactions entered into with wholly-owned subsidiaries, and may also provide that companies may seek shareholder approval for an exemption from

the requirement to provide an independent third party report for certain clearly defined types of recurrent transactions with an identified related party for a period of no longer than 12 months;

- proxy advisors must adopt measures to guarantee that their voting recommendations are accurate and reliable, based on a thorough analysis of all available information and unaffected by any existing or potential conflict of interest or business relationship. They must also publicly disclose certain key information relating to the preparation of their voting recommendations and, to their clients and the companies concerned, information on any conflict of interest that might influence their voting recommendations;
- intermediaries must offer companies the right to have their shareholders identified, rapidly transmit information relating to shareholders and facilitate the exercise of shareholder rights; and
- institutional investors and asset managers must, on a comply-or-explain basis, disclose their voting and engagement policies and certain aspects of asset management arrangements.

The proposal will be forwarded to the Parliament and the Council under the ordinary legislative procedure. The draft provides that member states will be required to implement the directive 18 months after its entry into force.

The proposal is available at:

http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=COM:2014:213:FIN&rid=5

Corporate Social Responsibility – European Commission Consults on Direction of EU Policy After 2014

The European Commission, on 29 April 2014, launched a public consultation in order to receive feedback on the implementation of its most recent policy on Corporate Social Responsibility ("CSR"), which is outlined in the 2011 Communication, *A Renewed EU Strategy 2011-14 for Corporate Social Responsibility*.

The consultation aims in particular to receive feedback on the various activity streams included in the 2011 CSR Communication in order to learn whether they were useful, successful or whether specific actions were missing. It also aims to receive input about what future challenges exist in CSR and what prospective activities might be required.

The consultation will run until 15 August 2014, and contributions should be made via an online questionnaire. The results of the consultation will feed into a multi-stakeholder forum on CSR, which is planned for November 2014.

The consultation is available at:

http://ec.europa.eu/enterprise/policies/sustainable-business/corporate-social-responsibility/public-consultation/index_en.htm

The press release is available at:

http://europa.eu/rapid/press-release_IP-14-491_en.htm

European Commission Consults on Definition of FX Financial Instruments

On 11 April 2014, the European Commission published a consultation paper on the definition of foreign currency exchange ("FX") financial instruments. The consultation responds to concerns expressed about the lack of harmonisation between EU Member States on the definitions of an FX financial instrument and a spot FX contract. The purpose of the consultation is to assist the Commission in preparing a formal proposal. The consultation includes ten questions which range from the use of FX, settlement periods, developments in the FX market, risks, transitional periods and interaction with regimes outside of the EU. Responses to the consultation are due on 9 May 2014.

The consultation webpage is available at:

http://ec.europa.eu/internal_market/consultations/2014/foreign-exchange/index_en.htm

European Supervisory Authorities Consult on Draft RTS on Risk Mitigation for OTC Derivatives

On 14 April 2014, the Joint Committee of the European Supervisory launched a consultation on draft RTS on risk mitigation for OTC derivatives as required under the European Market Infrastructure Regulation ("EMIR"). EMIR requires parties to derivative contracts that are not cleared through a central counterparty to use risk mitigation techniques. The draft RTS set out risk management procedures for the timely, accurate and appropriately segregated exchange of collateral, procedures for intragroup exemptions and the criteria for identifying practical and legal impediments to the prompt transfer of funds between counterparties.

Responses to the consultation are due by 14 July 2014. The European Supervisory Authorities will prepare final draft RTS for submission to the European Commission by the end of 2014. It is proposed that the RTS will enter into force on 1 December 2015, with a phase-in period of four years to mitigate the impact on liquidity. It is intended that the requirements will apply to market participants with an aggregate month-end average notional amount of OTC derivatives exceeding €3 trillion from that date. From 1 December 2019, the requirements would apply to any counterparty which is part of a group whose aggregate month-end average notional amount of OTC derivatives exceeds €8 billion.

The consultation paper is available at:

http://www.eba.europa.eu/documents/10180/655149/JC+CP+2014+03+%28CP+on+risk+mitigation+for+OTC+derivatives%29.pdf

ESMA Advances Intention to Ease Frontloading Requirements Under EMIR

On 8 May 2014, ESMA sent a letter to the European Commission in relation to its intention to ease certain front-loading requirements under EMIR. Front-loading refers to clearing obligations under EMIR, which require counterparties to centrally clear certain derivative trades entered into after a central counterparty has been authorised under EMIR to clear such transactions but before the EMIR clearing obligation comes into force. ESMA has informed the Commission that it plans to establish the front-loading requirements in a way that will minimise uncertainty. ESMA believes that the front-loading procedure can create uncertainties for derivatives end-users in situations where precise terms of a clearing obligation have not yet been defined, which can cause an adverse impact on risk hedging and financial stability.

ESMA's letter to the Commission is available at:

http://www.esma.europa.eu/system/files/2014-483_letter_to_european_commission_re_frontloading_requirement_under_emir.pdf

GERMAN DEVELOPMENTS

Regional Court of Munich Orders Former Managing Board Member of Siemens AG to Pay €15 Million in Damages for Failure to Implement Compliance System

On 10 December 2013, the Regional Court of Munich I (*Landgericht München I*) issued a judgment ordering a former management board member of Siemens AG to pay €15 million in damages to Siemens AG. The judgment has been appealed by the defendant.

The defendant, Heinz Joachim Neuburger, served as a management board member of Siemens AG from 1998 until 2006. During this time, Siemens AG operated a system of secret “black accounts” that were used to pay bribes to foreign government officials. As a consequence, the matter was investigated by the SEC, Siemens AG was required to pay significant fines and Siemens AG retained a law firm to investigate the matter. Thereafter, Siemens AG sought to recover damages from former management board members. While other former management board members reached out of court settlements with Siemens AG, Mr. Neuburger refused to settle. Thus, Siemens AG initiated suit against Mr. Neuburger seeking damages for the legal fees charged by the law firm hired to investigate the bribery system.

The court reasoned that management board members must act with the care of a diligent and conscientious manager pursuant to Section 93 para. 1 of the German Stock Corporation Act (*Aktiengesetz*). Moreover, the court explained that a management board member may not order actions which are in violation of the law and must ensure that no laws are violated. Further, the Court reasoned that Section 91 para. 2 of the Stock Corporation Act specifies that a compliance system must be established which is suitable to discover developments which put the company at risk, which include violations of the law. The court explained that the establishment of such a compliance system must take into account the company’s size, the type of business pursued, the internal organisation, the geographic scope and suspected transgressions in the past.

Under German corporate law, the management board has a collective obligation to run the company with diligence and conscientious care. Thus, the management board member was not successful in asserting that the management board members did not follow his ideas and proposals. In this regard, the Court explained that while a management board member must generally implement board resolutions even if the member voted against such resolution, this does not apply to resolutions which violate the law. Further, the court explained that it must be assumed that the need to implement measures to increase compliance was apparent at the relevant time and that inaction was thus unlawful. Under such circumstances, the Court explained, a management board member would have needed to object and, if necessary, inform the supervisory board.

German Federal Court of Justice Rules on Shareholder’s Information Rights and European Shareholder’s Rights Directive

In its order dated 5 November 2013, the German Federal Court of Justice (*Bundesgerichtshof* (BGH)) confirmed that pursuant to German corporate law, the managing board of a German stock corporation (*Aktiengesellschaft*) is only obliged to answer questions by shareholders on agenda items to the extent an answer is necessary for a reasonable assessment of the agenda items. In particular, the court held that provisions limiting the information right of shareholders at a shareholders’ meeting is in compliance with regulation 2007/36/EC (Shareholder’s Rights Regulation). Sec. 131 para. 1 of the German Stock Corporation Act (*Aktiengesetz*) provides that upon request of a shareholder, the management board of a German corporation (*Aktiengesellschaft*) must provide information to the shareholder on agenda items to the extent such information is necessary for a reasonable assessment of the agenda item. Art. 9 para. 1 of the Shareholder’s Rights Directive provides that the member states must enable each shareholder to ask questions on agenda items and that the corporation must answer such questions. The Court explained that the information right pursuant to Art. 9 para. 1 extends to information on agenda items beyond the scope of what is necessary for a reasonable assessment of the agenda item. However, the court reasoned that measures which member states may take to ensure the good order of general meetings pursuant to Art. 9 para. 2 of the Shareholder’s Rights Directive allow limiting a shareholder’s information right to information which is necessary for a reasonable assessment of an agenda item. Citing European legislative history on the Shareholder’s Rights Directive, the Court held that this interpretation was clear and refused to refer the case to the European Court of Justice.

UK DEVELOPMENTS

ABI Recommendations on Lock-Up Agreements

On 14 April 2014, the Association of British Insurers ("ABI") published its recommended best practice approach in relation to lock-up agreements. The advice focuses on lock-up agreements entered into by investors with significant shareholdings at the time of an IPO or secondary placing with lock-ups that may be waived at the sole discretion of the underwriting banks. The ABI notes that increasingly lock-ups are being waived before the stated expiry date and in some cases a long time before.

ABI recommends that:

- the period of the lock-up, and the circumstances in which a sale may take place prior to its expiry, should be clearly disclosed;
- the appropriate period and terms of a lock-up will depend on the circumstances; however, in general:
  - soft lock-ups (*i.e.*, where the lock-up may be waived at the sole discretion of the investment bank) are only appropriate for periods of relatively short duration;
  - for lock-ups of a longer duration it is appropriate for the lock-up agreement to specify an initial period of hard lock-up (*i.e.*, a period during which the lock-up may only be waived in objectively definable circumstances); and
  - any waiver at the sole discretion of the banks should only be given after careful consideration, taking full account of the overall merits from the perspective of investors and the need to maintain market integrity. Any such waiver would generally only be expected at a time close to the stated expiry of the lock-up.

ABI's advice is available at:
https://www.abi.org.uk/~/media/Files/Documents/Publications/Public/2014/investment/ABI%20Position%20on%20Lock%20Up%20Agreement%20April%202014.ashx

Government Responses to BIS Transparency and Trust Discussion Paper: Small Business, Enterprise and Employment Bill

On 21 April 2014, the Department for Business Innovation & Skills ("BIS") published the government's responses to its discussion paper, "Transparency & Trust: Enhancing the transparency of UK company ownership and increasing trust in UK business". These proposals have been included in the government's Small Business, Enterprise and Employment Bill (the "Bill"). The Bill includes various amendments to the Companies Act 2006, including to:

- require companies to identify those persons with significant control over the company and keep a publicly available register of those persons;
- prevent the creation of new bearer shares and require existing bearer shareholders to surrender their shares to the company in exchange for registered shares;
- prohibit the use of corporate directors by UK companies, subject to limited exceptions;
- replace the current requirement for an annual return with an obligation to confirm at least once in a 12 month period that all requisite information has been delivered to the Companies House;

- replace the requirement for the statement of capital to specify the paid up and unpaid amounts on each share, instead imposing a requirement to state the aggregate amount unpaid on the total number of shares; and
- give private companies the option of holding statutory registers (e.g. register of directors, directors' residential addresses, members and secretaries) on a public register instead.

The Bill also amends the Company Directors Disqualification Act 1986 to expand the matters a court should have regard to when deciding whether to disqualify a director.

Earlier discussions on these developments can be found in our previous newsletter published in October 2013.

A copy of the Bill is available at:

http://www.publications.parliament.uk/pa/bills/cbill/2014-2015/0011/cbill_2014-20150011_en_1.htm

The government's April 2014 response is available at:
https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/304297/bis-14-672-transparency-and-trust-consultation-response.pdf

FRC Consultation on the UK Corporate Governance Code

On 24 April 2014, the Financial Reporting Council ("FRC") published a consultation document on its two yearly review of possible changes to the UK Corporate Governance Code. The FRC's proposed amendments include:

- ensuring remuneration policies are designed with the long-term success of the company in mind;
- ensuring companies put arrangements in place that will enable them to recover or withhold variable pay, and encouraging companies to give further consideration to the arrangements they have in place for deferred consideration, such as vesting and holding periods for shares;
- when announcing the results of the AGM, a company that has received a significant vote – and the FRC consultation document does not offer a definition of "significant" for these purposes – against any resolution should explain what action it intends to take to understand the reason behind the result; and
- requiring companies to state in their financial statements whether they have considered it appropriate to adopt the going concern basis of accounting.

The proposed changes will apply to financial years beginning on or after 1 October 2014.

The consultation paper is available at:

https://www.frc.org.uk/Our-Work/Publications/Corporate-Governance/Proposed-Revisions-to-the-UK-Corporate-Governance-File.pdf

The press release to the consultation paper is available at:

https://www.frc.org.uk/News-and-Events/FRC-Press/Press/2014/April/Consultation-on-the-UK-Corporate-Governance-Code-p.aspx

Narrative Reporting: ICSA Consultation on Annual Report Contents

Following a request from BIS, the Institute of Chartered Secretaries and Administrators ("ICSA") has published a consultation on a contents list for company annual reports.

The list aims to assist those preparing reports and is intended for UK listed companies.

The consultation paper is available at:

https://www.icsa.org.uk/assets/files/annual-report-consultation-april-2014.pdf

Accounting Directive: Supplement to Consultation on Implementation on Extractive Industries Reporting Requirements

On 2 May 2014, BIS published a paper giving supplementary information on the government's consultation on the implementation of the extractive reporting requirements in Chapter 10 of the EU Accounting Directive, which was launched on 28 March 2014. The paper provides an update on issues that have been raised in responses to the consultation. BIS has clarified that:

- the definition of "mining or quarrying undertaking" in the draft Reports on Payments to Governments Regulations 2014 will be amended following the consultation to bring it in closer alignment with the Accounting Directive; and
- the government intends to consider how to amend the draft regulations to make it clear that parent companies are required to prepare a report for any of its subsidiaries undertaking extractive activities that are within scope, and intends to amend the regulations to make it clear that all relevant undertakings within a group would fall in scope regardless of the location.

The supplementary information to the consultation paper is available at:

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/307982/bis-14-786-uk-implementation-eu-accounting-directive__-_supplementary_information.pdf

The consultation paper is available at:

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/299454/bis-14-622-uk-implementation-of-the-eu-accounting-directive-chapter-10-extractive-industries-reporting-consultation.pdf

FCA Publishes Revised Listing Rules and Amendments to DEPP

On 6 May 2014, the FCA published Listing Rules (Listing Rules Enhancements) Instrument 2014 (the "Instrument") to amend the FCA Handbook and the Listing Rules with effect from 16 May 2014. The Instrument implements the majority of the consultation proposals included in the FCA's Consultation Paper CP 13/15 on Enhancing the Effectiveness of the Listing Regime, including the introduction of new initial and ongoing requirements for premium listed companies with a controlling shareholder and new and revised Listing Principles. On 16 May 2014, the FCA published Policy Statement PS14/8 setting out its response to its consultation in CP 13/15.

Earlier discussions on these developments can be found in several previous newsletters, including those of October 2012 and January 2014.

The Instrument is available at:

http://media.fshandbook.info/latestNews/FCA_2014_33.pdf

The Policy Statement is available at:

http://www.fca.org.uk/static/documents/policy-statements/ps14-08.pdf

Consultation on Amendments to the Walker Guidelines for Portfolio Companies

On 8 May 2014, the Guidelines Monitoring Group ("GMG") published a consultation paper setting out proposed amendments to the Walker Guidelines to reflect changes introduced by the Companies Act 2006 (Strategic Report and

Directors' Report) Regulations 2013. The GMG makes a number of proposals, including to require the inclusion of a specific statement of conformity with the Guidelines in the annual report of the portfolio company (or an explanation for areas of noncompliance). The GMG also concluded that it will not be necessary to extend the enhanced disclosure requirements for portfolio companies to include details on greenhouse gas emissions.

The proposed changes will affect portfolio companies with accounting periods ending on or after 30 September 2014. Portfolio companies with accounting periods ending on or after 30 September 2013 may voluntarily include the additional information if they wish.

The consultation paper is available at:

http://walker-gmg.co.uk/sites/10051/files/gmg_guidelines-apr14_final.pdf

Revised AIM Rules for Companies and Nomads

On 13 May 2014, the London Stock Exchange (the "Exchange") issued AIM Notice 39 to confirm changes to the AIM Rules for Companies (the "Aim Rules") and AIM Rules for Nominated Advisers (the "Nomad Rules"). Key changes to the AIM Rules include additional guidance relating to the disclosure of price sensitive information, and clarification that the requirement for shareholder consent for an AIM cancellation may be waived for a scheme of arrangement if it has been sanctioned by the courts and approved by shareholders. The AIM Rules also expand on the list of information that must be available on a website to include (among others):

- the date on which the details relating to the AIM securities in issue and significant shareholders was last updated;
- the annual accounts published under AIM Rule 19 for the last three years or since admission, whichever is the lesser;
- whether the AIM company is subject to the UK Takeover Code or any other similar legislation or code in its country of incorporation or operation, or any other similar provisions it has voluntarily adopted; and
- details of the corporate governance code that the AIM company has decided to apply, how it complies with that code, or if no code has been adopted, disclosure of that fact.

The key changes to the Nomad Rules include a change to Nomad Rule 11, so that a Nominated Adviser will only be required to inform the Exchange of a potential change of control which is reasonably likely.

AIM Notice 39 is available at:

http://www.londonstockexchange.com/companies-and-advisors/aim/advisers/aim-notices/aimnotice39.pdf

The AIM Rules are available at:

http://www.londonstockexchange.com/companies-and-advisors/aim/advisers/aim-notices/aimrulescompaniesmay2014.pdf

The Nomad Rules are available at:

http://www.londonstockexchange.com/companies-and-advisors/aim/advisers/aim-notices/aimrulesnomadsmay14.pdf

FSMA 2000 (Transparency) Regulations 2014 Laid Before Parliament

On 16 May 2014, the Financial Services and Markets Act 2000 (Transparency) Regulations 2014 were laid before Parliament. The regulations will allow the FCA to remove from the Transparency Rules the requirement for share issuers to produce interim management statements or quarterly reports. The regulations implement Directive

2013/50/EU which makes various amendments to the Transparency Directive (the "Amending Directive"). The transposition deadline for implementing the Amending Directive into UK law is 26 November 2015, but the government has stated that it intends to remove the quarterly reporting requirements before the deadline.

The explanatory memorandum to the regulations is available at:
http://www.legislation.gov.uk/uksi/2014/1261/pdfs/uksiem_20141261_en.pdf

Audit: Institutional Investor Committee Guidance on Audit Tendering

On 29 May 2014, the Institutional Investor Committee (made up of representatives from ABI, IMA and NAPF) published guidance for audit committees when companies put their audit contracts out to tender. The areas addressed by the guidance include transparency when companies decide to tender, identifying tender candidates, the tender process and selection criteria and audit firms' transparency when they cease to hold office.

The paper published by the Institutional Investor Committee is available at:
http://www.iicomm.org/docs/IIC_The_Audit_Tendering_Process.pdf

Narrative Reporting: FRC Final Guidance on the Strategic Report

On 9 June 2014, the FRC 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 (the "Regulations"). The Regulations came into force on 1 October 2013 and require certain companies to prepare a standalone strategic report as part of their annual report. The guidance is aimed at directors and is intended to serve as a best practice guide for entities preparing strategic reports. Further initiatives, including a review of progress towards clear and concise reporting in the 2014 reporting cycle, will be delivered by the FRC during 2014 and beyond.

The press release is available at:

https://www.frc.org.uk/News-and-Events/FRC-Press/Press/2014/June/FRC%E2%80%99s-work-to-encourage-clear-and-concise-reportin.aspx

The guidance is available at:

https://www.frc.org.uk/Our-Work/Publications/Accounting-and-Reporting-Policy/Guidance-on-the-Strategic-Report.pdf

True and Fair View: FRC Statement

On 4 June 2014, the FRC published an updated statement on the application of the true and fair view requirement for accounts prepared under IFRS and UK GAAP. BIS and the FRC confirmed, in October 2013, that the current legal framework requires companies to present a true and fair view. Whilst the recent statement is largely based on the FRC's 2011 statement it has been revised to reflect developments in UK GAAP and developments in EU audit legislation. The amendments have been made to address concerns raised in relation to the operation of the true and fair override in IFRS and the removal of the term prudence from the IFRS Conceptual Framework.

FRC confirms that in the majority of cases a true and fair view will be achieved by compliance with accounting standards and by additional disclosure to fully explain an issue. However, where compliance with an accounting standard would result in accounts being so misleading that they would conflict with the objectives of financial statements, the standard should be overridden.

The press release is available at:

https://www.frc.org.uk/News-and-Events/FRC-Press/Press/2014/June/FRC-publishes-'True-and-Fair'-statement.aspx
Martin Moore QC's opinion on the "true and fair" requirement is available at:
https://www.frc.org.uk/Our-Work/Publications/Accounting-and-Reporting-Policy/Martin-Moore-QC-Opinion-3-October-2013.pdf

Market Abuse: Government Review into the Operation of Wholesale Financial Markets

On 12 June 2014, HM Treasury, the Bank of England and the FCA announced the Fair and Effective Financial Markets Review, a review into the way wholesale markets operate. The review will consider and recommend, among other things:

- principles to govern the operation of fair and effective financial markets (taking account of existing rules and regulations);
- reforms to ensure standards of behaviour for firms within those markets are in accordance with those principles; and
- tools to strengthen the oversight of market conduct within both regulated and unregulated markets.

A final report will be issued in June 2015.

The press release for the review is available at:

https://www.gov.uk/government/news/fair-and-effective-markets-review-announced-by-chancellor-of-the-exchequer

The terms of reference for the review are available at:

https://www.gov.uk/government/publications/fair-and-effective-markets-review-terms-of-reference/fair-and-effective-financial-markets-review-terms-of-reference

Market Abuse: Improper Disclosure

In the recent Upper Tribunal case of Ian Hannam v FCA, it was found that Mr Hannam, then Global Co-Head of UK Capital Markets at JP Morgan Cazenove, engaged in market abuse by disclosing inside information other than in the proper course of the exercise of his employment within the meaning of section 118(3) FSMA. The Tribunal came to the following conclusions as to the meaning of inside information:

- a statement or communication need not be wholly accurate to be inside information, provided it indicates circumstances or events which actually exist or have occurred or could reasonably be expected to occur;
- where a statement indicates existing or past events, the FCA must prove they exist or have occurred. Where it indicates future events, the FCA must prove there is a realistic prospect that will occur;
- a statement by an insider which indicates a genuinely and reasonably held belief on the part of an issuer is capable of constituting inside information even if the belief subsequently turns out to be mistaken;
- the information must indicate a direction of movement in the price, but does not need to indicate the extent to which the price would or might be affected; and
- the reasonable investor test is not an exhaustive test of price sensitivity – the likely effect on price must be taken into account in applying the reasonable investor test. Instead there must be a real prospect of the information having a significant (*i.e.*, more than de minimis) effect on the price.

The decision also considers the scope of the ability to delay the announcement of inside information. The Tribunal accepted that a listed company could delay in order to allow for a period of verification to ensure that when an announcement is made it is not inaccurate or misleading.

In order to rely on the exception permitting disclosure in the normal course of the exercise of employment:

- the exception must be strictly construed;
- it can never be in the proper course of a person's employment for him to disclose inside information to a third party, where he knows that his employer and client would not consent to the disclosure of that information, unless he knows the recipient is under a duty of confidentiality and he knows the recipient knows that to be the case; and
- it will rarely be reasonable to disclose information in breach of the Takeover Code (*i.e.*, to disclose information regarding a prospective takeover bid).

The judgment is available at:

http://www.tribunals.gov.uk/financeandtax/Documents/decisions/Hannam-v-FCA.pdf

PIRC UK Shareholder Voting Guidelines 2014

The Pensions Investment Research Consultants ("PIRC") has published the 18th edition of its UK Shareholder Voting Guidelines, replacing the version published in February 2013. The guidelines contain a number of significant revisions in light of recent regulatory developments, including several revisions to the area of directors' remuneration.

Key changes in the most recent edition include:

- advice to shareholders on the new binding vote on remuneration policy;
- new recommendations and guidelines in relation to the disclosures required in the directors' remuneration report;
- revised guidelines on the balance between executive pay and financial performance of the company. In formulating its assessment PIRC will compare the percentage change in CEO pay over the last five year period against the percentage change in total shareholder return. PIRC will also apply a threshold of 200 per cent. of salary in informing its view of whether variable pay is excessive;
- new recommendations relating to corporate responsibility reporting in the strategic report; and
- new recommendations aimed at preserving the right of personal attendance at shareholder meetings.

The PIRC Guidelines are available to purchase at:

http://pirc.co.uk/news-and-resources2/guidelines

US DEVELOPMENTS

SEC Developments

SEC Staff Issues Statement on Effect of Court Decision on Conflict Minerals Rule

On 29 April 2014, the SEC Division of Corporation Finance issued a statement on the effect of a recent decision by the US Court of Appeals for the District of Columbia Circuit (the "Court") on the SEC's reporting requirements regarding conflict minerals originating in the DRC and adjoining countries (the "Conflict Minerals Rule").

The Court had concluded that Section 13(p)(1) of the Securities Exchange Act of 1934 (the "Exchange Act"), adopted pursuant to Section 1502 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "Dodd-Frank Act"), and the Conflict Minerals Rule "violate the First Amendment to the extent the statute and rule require regulated entities to report to the Commission and to state on their website that any of their products have 'not been found to be 'DRC conflict free'.'"

The statement issued by the Division of Corporation Finance on 29 April 2014 provided the following guidance:

- The 2 June 2014 deadline for issuers to file any reports required under the Conflict Minerals Rule remained in effect;
- The Form SD and any related Conflict Minerals Report should comply with and address those portions of the Conflict Minerals Rule that the Court upheld;
- Companies that are not required to file a Conflict Minerals Report should disclose their reasonable country of origin inquiry and briefly describe the inquiry they undertook; and
- Companies that are required to file a Conflict Minerals Report should include a description of the due diligence that the company undertook. If, after exercising due diligence, the company determines that any of its products have not been found to be "DRC conflict free" or if the company is unable to determine whether or not a product qualifies as "DRC conflict free," the company does not need to identify the products as "DRC conflict undeterminable" or "not found to be 'DRC conflict free,'" but should disclose, for those products, the facilities used to produce the conflict minerals, the country of origin of the minerals and the efforts to determine the mine or location of origin.

No company is required to describe its products as "DRC conflict free", having "not been found to be 'DRC conflict free'", or "DRC conflict undeterminable". If a company voluntarily elects to describe any of its products as "DRC conflict free" in its Conflict Minerals Report, it would be permitted to do so provided it had obtained an independent private sector audit as required by the rule. Pending further action, such a report will not be required unless a company voluntarily elects to describe a product as "DRC conflict free" in its Conflict Minerals Report.

Our related client publication is available at:

http://www.shearman.com/~/media/Files/NewsInsights/Publications/2014/04/SEC-Statement-on-Effect-of-Court-Decision-on-Conflict-Minerals-Rule-CM-043014.pdf

SEC Issues Guidelines on Using Social Media in Registered Securities Offerings

On 21 April 2014, the Staff of the Division of Corporation Finance of the SEC (the "Staff") released guidance to facilitate the use of social media for certain communications in registered securities offerings.

Recognising the interest in using technologies such as social media to communicate with security holders and potential investors, this guidance permits offering participants to use Twitter or other similar social media with character limitations to issue Rule 134 offering announcements and Rule 433 free writing prospectuses with respect to registered securities offerings.

Under the new SEC Staff guidance, offering participants are permitted to electronically communicate Rule 134 announcements and Rule 433 free writing prospectuses if:

- the electronic communication is distributed through a platform that has technological limitations on the number of characters or amount of text that may be included in the communication (e.g., Twitter);
- including the required statements in their entirety, together with the other information, the communication would exceed the limit on the number of characters or amount of text; and

- the communication contains an active hyperlink to the required statements and prominently conveys, through introductory language or otherwise, that important or required information is provided through the hyperlink.

The Staff also addressed the situation where an issuer distributes an electronic communication in compliance with Rule 134 or Rule 433 under the Securities Act of 1933 and a third party that is not an offering participant re-transmits that communication. This may arise in the context of some electronic communication platforms, such as those made available through certain social media websites, that permit users to re-transmit a posting or message they receive from another party. The Staff clarified its position that if the third party is neither an offering participant nor acting on behalf of the issuer or an offering participant and the issuer has no involvement in the third party's re-transmission beyond having initially prepared and distributed the communication in compliance with either Rule 134 or Rule 433, the re-transmission would not be attributable to the issuer.

The guidelines are available at:

http://www.sec.gov/divisions/corpfin/guidance/securitiesactrules-interps.htm#110-01

PCAOB Adopts Auditing Standard and Amendments

On 10 June 2014, the Public Company Accounting Oversight Board ("PCAOB") adopted a new auditing standard and amendments to its auditing standards to strengthen auditor performance requirements in the following three areas that historically have represented increased risks of material misstatement in company financial statements:

- related party transactions;
- significant transactions that are outside the normal course of business for the company or that otherwise appear to be unusual due to their timing, size, or nature; and
- financial relationships and transactions with its executive officers.

The guidelines are available at:

http://pcaobus.org/Rules/Rulemaking/Docket038/Release_2014_002_Related_Parties.pdf

Noteworthy US Securities Law Litigation

Halliburton Corporation, et al., v. Erica P. John Fund, Inc.: Supreme Court Upholds Fraud-on-the-Market Presumption but Allows "Price Impact" Rebuttals at Class Certification Stage

On 23 June 2014, the US Supreme Court reached a long-awaited decision in *Halliburton Corporation v. Erica P. John Fund*. The Court affirmed the continued validity of the fraud-on-the-market presumption that allows plaintiffs to plead reliance in the class action context, but gave defendants a new way to rebut that presumption at the class certification stage.

Rule 23 of the Federal Rules of Civil Procedure requires plaintiffs seeking to certify a case for class action treatment to show, among other things, that common questions of law or fact predominate across the class over questions affecting potential class members individually. In *Basic v. Levinson* (1988), the Supreme Court rejected the argument that each purported class member in a securities class action brought under Section 10(b) of the Exchange Act must prove that he or she relied individually on the defendant's alleged misrepresentations or omissions when purchasing the security. That standard would have made securities claims unsuitable for class treatment because of the individualised nature of questions of reliance. The Court in *Basic* held instead, based on the economic theory known as the efficient-capital-

markets hypothesis—which provides that prices of shares traded on well-developed markets reflect material, publicly available information—that plaintiffs can be presumed to have relied on material public misrepresentations when making their stock trades.

In *Halliburton*, the Court refused to overrule *Basic*, thereby affirming the validity of the presumption of reliance, because "[e]ven the foremost critics of the efficient-capital-markets hypothesis acknowledge that public information generally affects stock prices." The Court also ruled that the *Basic* presumption is consistent with the rule that plaintiffs must prove the requirements for class certification because plaintiffs must still prove the prerequisites (other than materiality) for applying the presumption. The Court declined to hold that plaintiffs must prove at the class certification stage that the alleged misstatements impacted the price of the stock—one of the main premises underlying the Basic presumption. But the Court ruled that defendants may present evidence to show a lack of "price impact" at the class certification stage—something that the lower court held could not be done until after a class is certified and the merits are being considered.

While *Halliburton* had the potential to upend securities fraud class actions by calling the *Basic* presumption into doubt, the Court largely left the prior legal landscape intact. But the Court's allowance for defendants to offer evidence of the lack of price impact at the class certification stage provides defendants with a new way to defeat securities class actions at this early stage, before feeling pressured to settle because of the size of potential damages after a class has been certified. Only time will tell whether this change in the landscape will have a significant impact on the outcome of securities class actions.

Further information on *Halliburton* is available at:

http://www.shearman.com/en/newsinsights/publications/2014/06/supreme-court-preserves-fraud-on-the-market

A related report, based on a multi-firm effort that we led before the case was decided, on the possible impact of the case is available at:

http://www.shearman.com/en/newsinsights/publications/2014/06/halliburton-on-securities-class-action-litigation

United States Securities and Exchange Commission v. Citigroup Global Markets, Inc.: Substantial Deference Must be Afforded to Civil Enforcement Settlements

On 4 June 2014, the federal appellate court in New York vacated the trial court's refusal to approve a settlement reached between the SEC and Citigroup. The appellate court thus lent support to private parties reaching settlements with government agencies such as the SEC on a compromise basis without admitting or denying fault.

In *Citigroup*, the SEC alleged that Citigroup violated the Securities Act of 1933 by claiming to investors that collateralised subprime mortgage-related investments were selected by an independent advisor when Citigroup itself put low-quality assets in the portfolio, against which Citigroup took a short position. The SEC and Citigroup reached a settlement by consent decree whereby Citigroup would pay $285 million in total, accept an injunction against further statutory violations, and temporarily change its internal practices. The district judge rejected the settlement because Citigroup neither admitted nor denied the facts alleged by the SEC. Without that information, the court reasoned, it would be "a mere handmaiden to a settlement privately negotiated on the basis of unknown facts, while the public is deprived of ever knowing the truth in a matter of obvious public importance."

The appellate court vacated the district court's decision because the lower court may not require the SEC to "establish the 'truth' of the allegations against a settling party" as a pre-condition to settlement. In addition, the lower court did not adequately defer to the SEC's determination as to whether the settlement harmed the public interest. While district courts might sometimes need additional facts before considering a settlement's fairness, the court's "primary focus . . .

should be on ensuring the consent decree is procedurally proper." The appellate court also noted the many discretionary factors that go into settlement decisions, which "are uniquely for the litigants to make." The appellate court therefore vacated the district court's decision and ordered the lower court to reassess the settlement in light of the appellate opinion.

The district court's initial refusal to approve the settlement in *Citigroup* garnered a lot of public attention and raised questions about how the decision would impact future civil enforcement actions. But the appellate ruling that courts should focus primarily on the procedures followed rather than on the truth of the underlying allegations goes a long way toward restoring the ability of parties to reach mutually agreeable compromises in civil enforcement actions without risking the negative impact of admissions on later litigation and without facing heightened uncertainty as to whether the court will ultimately approve the settlement.

City of Pontiac Policemen's & Firemen's Ret. Sys. v. UBS AG, et al.: Morrison Precludes Claims Based on the "Listing Theory" for Securities That are Cross-Listed on a US Exchange

On 6 May 2014, the federal appellate court in New York considered two questions of first impression arising out of the US Supreme Court's landmark decision in *Morrison v. National Australia Bank* precluding certain extraterritorial applications of Section 10(b) of the Exchange Act. The court here considered whether *Morrison* bars such claims related to (1) foreign-issued securities that were purchased by foreign plaintiffs on a foreign exchange, but were cross-listed on a domestic exchange (*i.e.,* the "listing theory") and (2) US investors who purchased foreign securities on a foreign exchange through a buy order that was placed in the US The court in *City of Pontiac* held that *Morrison* precludes both types of claims.

In *Morrison*, the Supreme Court ruled that Section 10(b) does not apply extraterritorially to so-called "foreign-cubed" claims—*i.e.*, claims where "(1) *foreign* plaintiffs [are] suing (2) a foreign issuer in an American court for violations of American securities laws *based* on securities transactions in (3) foreign countries." The court in *City of Pontiac* explained why, based on *Morrison's* underlying rationale, two new factual variations that were not considered in *Morrison* are also not allowed. *Morrison* does not allow claims by foreign investors based on foreign securities that are cross-listed on a US exchange because *Morrison's* focus is on "the location of the securities transaction and not the location of an exchange where the security may be dually listed." The court in *City of Pontiac* also ruled that Section 10(b) does not apply to the "mere placement of a buy order" in the US by a US entity to purchase foreign securities on a foreign exchange. Using the standard from a recent ruling, the court reasoned that a buy order being placed in the US does not mean that the buyer incurs "irrevocable liability" within the US when the transaction is then executed on a foreign exchange. Moreover, "a purchaser's citizenship or residency does not affect where a transaction occurs."

Taken together, these two novel applications of *Morrison* should give further comfort to parties transacting in foreign securities on foreign exchanges that Section 10(b) applies only to truly domestic transactions. The fact that the securities are concurrently listed on a US exchange, that the purchaser is a US entity, or even that the buy order is placed in the US are not enough (at least according to the federal appellate court in New York) to bring foreign transactions within the ambit of Section 10(b).

Further information on *City of Pontiac* is available at:

http://www.shearman.com/en/newsinsights/publications/2014/05/second-circuit-rejects-listing-theory

Recent SEC/DOJ Enforcement Matters

In the Matter of Paradigm Capital Management, SEC File No. 3-15930: SEC Reaches Settlement in First Whistleblower Anti-Retaliation Claim Under the Dodd-Frank Act

On 16 June 2014, the SEC announced the settlement of a case concerning workplace retaliation against a whistleblower and the underlying allegations that the whistleblower reported. This is the first action to be brought under the whistleblower anti-retaliation provision of the securities regulatory scheme enacted through the Dodd-Frank Act in response to the recent financial crisis.

This action arose out of a whistleblower's report to the SEC that a hedge fund adviser and its owner engaged in improperly disclosed principal transactions. The whistleblower, who was the fund's head trader, reported these activities in late March 2012. Starting in July 2012, after the whistleblower revealed to the hedge fund owner that he reported the principal transactions to the SEC, the whistleblower was subjected to several adverse employment actions, including being demoted from head trader, tasked with investigating the conduct he complained of, and generally being marginalised at work. All of these actions culminated in the whistleblower resigning from his job in August 2012.

The settlement with the SEC states that the company violated the anti-retaliation provision of the Exchange Act by taking adverse employment actions against the whistleblower because of his report to the SEC. In addition, the settlement lists violations related to the underlying conduct at issue. In order to settle the charges, the company and owner agreed to pay $2.2 million and the company agreed to hire an independent compliance consultant.

This action highlights the SEC's new whistleblower enforcement power under the Dodd-Frank Act. The chief of the SEC's whistleblower office explained in a press release that "[f]or whistleblowers to come forward, they must feel assured that they're protected from retaliation . . . . We will continue to exercise our anti-retaliation authority . . . where a whistleblower is wrongfully targeted for doing the right thing and reporting a possible securities law violation." This matter suggests that in addition to other types of whistleblower-related enforcement actions, the SEC is ready to pursue retaliation claims when adverse employment actions are taken against whistleblowers. Companies should consult counsel on how to avoid taking actions vis-a-vis known or suspected whistleblowers that might be perceived or portrayed as retaliatory.

Employment Benefits Updates

OSHA Issues Interim Final Rule on Whistleblower Procedures Under the Consumer Financial Protection Act

On 3 April 2014, the US Department of Labor's Occupational Safety and Health Administration ("OSHA") issued its interim final rule and request for comments on the procedures for handling retaliation complaints under the Consumer Financial Protection Act (the "CFPA"). The interim rule went into effect immediately and applies to employers engaged in offering or providing a financial product or service, including residential mortgages, mortgage loan modification and foreclosure relief services, private education loans, consumer credit, and debt relief services, and also applies to affiliates of such employers. These new procedural rules are in line with those applicable to other whistleblower protections that fall under OSHA's authority.

The CFPA was enacted as Title X of the Dodd-Frank Act. It created the Consumer Financial Protection Bureau (the "Bureau") as an independent bureau to regulate the offering and provision of consumer financial products or services under certain federal consumer financial laws.

Under the CFPA, covered employees in the consumer financial product and service industries are protected from retaliation for reporting violations of the CFPA. Under the final interim rules, an employee who believes that he or she has been retaliated against for a "protected activity" under the CFPA must file a complaint or make an oral complaint with OSHA within 180 days after the alleged violation.

Protected activity includes providing information regarding a violation of the CFPA or related law to the employer, the Bureau or state or local authority and refusing to participate in, any activity, policy, practice, or assigned task that the employee reasonably believes to be in violation of any rule under the jurisdiction of the Bureau.

In filing a complaint, the employee has the initial burden of establishing that the protected activity was a "contributing factor" in the retaliatory action; an employer then has the opportunity to rebut the claim by demonstrating with clear and convincing evidence that it would have taken the same adverse employment action had the employee not engaged in the protected activity.

The comment period closed on 2 June 2014. OSHA's interim final rule is available at:

http://www.regulations.gov/#!documentDetail;D=OSHA-2011-0540-0001

ASIAN DEVELOPMENTS

HKEx Publishes Revised Connected Transaction Rules

On 21 March 2014, The Stock Exchange of Hong Kong Limited (the "Stock Exchange") published amendments to the connected transaction rules under the Rules Governing the Listing of Securities on the Stock Exchange and the Rules Governing the Listing of Securities on the Growth Enterprise Market of the Stock Exchange (collectively the "Listing Rules"). The revised rules will take effect from 1 July 2014.

The revised rules follow a public consultation launched by the Stock Exchange in April 2013. The Stock Exchange has also taken the opportunity to rewrite the connected transaction rules in plain language and to align the definitions of "connected person" and "associate" used in various parts of the Listing Rules with those used for connected transactions where their purposes are to protect minority shareholders or avoid conflicts of interest.

Unless an exemption applies, a connected transaction is subject to the requirements of announcement, annual review and independent shareholders' approval. The revised rules aim to ease the compliance burden of listed issuers by simplifying the requirements and introducing new exemptions. Key changes include:

- Exemptions for Connected Persons at the Subsidiary Level

  Connected persons include directors, chief executives and substantial shareholders (10% or more) of a listed issuer or any of its subsidiaries. Under the Listing Rules, there are two levels of connected persons: "connected person at the issuer level" and "connected person at the subsidiary level". Taking into account that a connected person at the subsidiary level is less likely to be able to influence the decisions of a listed issuer, the Stock Exchange has amended the rules so that:

  - a transaction on normal commercial terms entered into between a listed issuer and a connected person at the subsidiary level will be exempt from the independent shareholders' approval requirement; and
  - a director, chief executive or substantial shareholder of an insignificant subsidiary will be excluded from the definition of "connected person". With the exclusion, transactions between a listed issuer and persons connected with insignificant subsidiaries would fall outside the connected transaction regime.

- Increase Monetary Limit for De minimis Transaction Exemption

Currently, a full exemption applies where a connected transaction is entered into on normal commercial terms and the relevant consideration ratio, assets ratio, revenue ratio and equity capital ratio are all:

- less than 0.1%;
- less than 1%, and the transaction is a connected transaction only because it involves connected persons at the subsidiary level; or
- less than 5%, and the total consideration is less than HK$1,000,000.

The monetary limit of HK$1,000,000 set out above will be increased to HK$3,000,000 under the revised rules.

- Removing the 1% Cap for the Exemption on Provision of Consumer Goods or Services

  The Stock Exchange has also modified the exemption which applies to a listed issuer buying or selling consumer goods or services. Under the current rules, the value of the transaction must be less than 1% of the listed group's total revenue or total purchases in order for the exemption to apply. The Stock Exchange has removed the 1% cap so that the exemption will apply irrespective of the transaction size so long as the other qualifying conditions are satisfied, e.g. the transaction must be on normal commercial terms and the goods or services must be of a type ordinarily supplied for private consumption.

- Exemptions for Indemnity or Insurance Against Directors' Liabilities

  New exemptions have been introduced allowing listed issuers to grant indemnities to directors and to purchase insurance for directors against liabilities incurred in the course of performing their duties, provided that the indemnity or insurance is permitted under Hong Kong law and the law of the place of incorporation of the issuer.

- Relaxing the Rules with Regard to Transactions With Third Parties

  Under the existing rules, connected transactions include certain acquisitions or disposals of interest in a target company from or to a third party where a shareholder of the target company is a director, chief executive or controlling shareholder (30% or more) of the listed issuer or any of its subsidiaries. The Stock Exchange has simplified the rules so that:

  - a disposal of interest in the target company by the listed issuer will no longer constitute a connected transaction; and
  - for acquisitions, the only type of transactions caught by the connected transaction rules is where a substantial shareholder of the target company is (or is proposed to be) a director, chief executive or controlling shareholder at the issuer level or an associate of any of them.

The revised connected transaction rules are available at:

Main Board:

http://www.hkex.com.hk/eng/rulesreg/listrules/mbrulesup/Documents/mb_contxn_1407.pdf

Growth Enterprise Market:

http://www.hkgem.com/listingrules/amendments/e20140701a.pdf

CONTACTS

This newsletter is intended only as a general discussion of these issues. It should not be regarded as legal advice. We would be pleased to provide additional details or advice about specific situations if desired.

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This memorandum is intended only as a general discussion of these issues. It should not be regarded as legal advice. We would be pleased to provide additional details or advice about specific situations if desired.

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