CORPORATE UPDATE JANUARY 2018

Welcome to our January 2018 edition of Corporate Update, our bi-annual bulletin in which we bring together the key developments in company law and corporate finance regulation which have occurred over the previous six months and consider how these might impact your business. In addition, we look ahead to forthcoming legal and regulatory changes.

CONTENTS

Key Topics

- Two important new reporting obligations must be met by qualifying companies in the first half of this year:
  - gender pay gap reporting; and
  - payment practices reporting.
- The General Data Protection Regulation will take direct effect in May this year – is your business ready?
- The FCA has imposed its first fine for breach of Article 17 of the Market Abuse Regulation (disclosure of inside information by a company).
- Upcoming legal and regulatory changes:
  - The FRC has published its proposals to amend the UK Corporate Governance Code.
  - The UK Business and Energy Secretary has announced major new proposals to enable the UK Government to intervene in mergers that raise national security concerns, even when they involve smaller businesses.
  - BEIS has consulted on proposed changes to Corporate Energy and Greenhouse Gas reporting intended to extend the reach of the current reporting regime.

CORPORATE GOVERNANCE AND NARRATIVE REPORTING UPDATE

Your 2018 AGM and beyond

In December 2017 we published our AGM Update for the 2018 AGM season, which highlights key considerations for listed companies to be aware of as they prepare for their 2018 AGM and move forward into a new financial reporting season. Key areas covered in the update include:

- upcoming narrative reporting changes arising from the Government's response to its Green Paper on corporate governance reform. In particular, we consider:
  - the FRC's consultation on proposed changes to the UK Corporate Governance Code;
  - new non-financial information statement requirements; and
  - new information to be included in the corporate governance statement on companies' diversity policies;
- a discussion on the practical application of new rules around virtual AGMs;
- the inclusion of disclosures in annual reports on the impact of Brexit; and
- changes affecting directors' remuneration in 2018 and the Investment Association's 2017 update to its remuneration principles.

If you have not yet received your 2018 AGM Update you can access a copy here.

It is worth noting that the Investment Association's (**IA**) register of listed companies that have encountered shareholder opposition of 20% or more on any resolution (referred to in the AGM Update) has now gone live. The IA reported on 19 December that over one fifth of FTSE all-share companies feature on the register following shareholder dissent in AGMs and general meetings held in 2017.

Gender Pay Gap Reporting – the first deadline looms

In our July 2017 Corporate Update, we highlighted The Equality Act 2010 (Gender Pay Gap Information) Regulations 2017 which require qualifying companies to report on their gender pay gaps (**GPG**) across salaries and bonuses throughout the business and in December 2017 ACAS published its finalised guidance on managing gender pay reporting (**ACAS Guidance**). The deadline for the initial GPG reports (which are based on a snapshot of pay data taken on 5 April 2017) is fast approaching and first reports must be published on or before 4 April 2018.

Relevant Employee

A relevant employee is a person who works for the company under a contract of employment, an apprenticeship or a personal contract to do work or provide services. The broad definition from the Equality Act 2010 means companies will usually have to include directly engaged self-employed contractors and workers in their headcount. Partners in traditional partnerships are excluded from the regulations. Agency workers will form part of the headcount of the agency that provides them and not the employer to which they are on assignment.

Who must report? All private sector employers with a headcount of 250 or more employees on 5 April 2017 (and on each 5 April going forwards). The obligation applies to each qualifying employer within a group, so, different employing entities in a group will each have to produce a GPG report; an aggregated report can be produced but not in place of the employing entity's individual report.

When must the GPG report be made? All relevant employers must analyse their gender pay gaps based on a snapshot of pay data taken on 5 April each year and report their data findings within 12 months of that date. The first report must be published on or before 4 April 2018.

Editor Comment:

Despite the ACAS guidance recommending that GPG reports are made as soon as possible after the April snapshot is taken, by midway through this month, it was reported that less than 7% of companies required to produce a GPG report on the government website had done so. We therefore expect to see a large amount of reporting activity in the coming weeks. As well as prioritising making the reports, companies should give some thought to what can be learnt from the data and what extra information may be helpful to explain it.

What GPG information needs to be included? Reports are to be compiled based on a snapshot of pay data taken, in respect of Relevant Employees, on 5 April each year and must set out:

- the difference between both the mean and the median hourly rates of pay for male and female Relevant Employees;
- the proportions of male and female Relevant Employees in the different quartiles of hourly rate of pay;
- the difference between the mean bonus paid to male and female Relevant Employees; and
- the proportion of male and female Relevant Employees who were paid a bonus.

The report must be accompanied by a written statement signed by a senior responsible person (e.g. a director) confirming the accuracy of the data being published.

Where must the GPG report be made available? The report must be on a searchable website that is accessible to the relevant employer's employees and the public. A link to this report must also be uploaded to the government-sponsored website together with the details of the person signing the compliance statement.

Sanctions for non-compliance: The Government proposes to produce publicly displayed tables, by sector, of employers' reported pay gaps. It has set out its intention to identify and highlight employers which publish particularly full and explanatory information and may also name and shame employers known not to have complied.

Whilst the GPG regulations do not impose civil or criminal penalties for non-compliance, the Equality and Human Rights Commission (**EHRC**) has confirmed that failure to comply would amount to an unlawful act under the Equality Act 2010, in relation to which it may take enforcement action. In the first instance it proposes to seek an informal resolution with defaulting employers, if resolution is not reached or

Mind the Gap

GPG information required by the regulations is important, but taken in isolation it may not enable the reader to truly understand the pay differences within a company and may, on its own, result in some unexplained anomalies. Whilst the GPG reporting is, at least in part, intended to help identify unlawful pay inequality within companies, this is not its sole purpose and it is acknowledged by the Government and ACAS that the existence of a pay gap does not itself suggest that there is unlawful pay inequality within the reporting entity. The causes of the pay gap could be attributable to this, but there are also many other factors that could be causative. To head off any suggestions of pay inequality we would advise that the narrative statement and/or internal communications outline the (suspected/known) causes of the 'gap'.

In addition, we would strongly encourage companies to carry out some further analysis beyond simply gathering the data required to be reported, to enable them to include an accompanying narrative statement, which may help contextualise the required disclosed data. Companies may want to consider including some of the following additional information in their reports as well:

- adjusted pay gap figure(s) to reflect the different gender demographic across pay grades;
- information in relation to the gender mix by pay grade, role, level or seniority; and
- information in relation to the bonus distribution according to pay grade, role, level or seniority.

there is continued non-compliance, the EHRC will apply to the court for an order requiring the employer to comply. Failure to comply with any such order without reasonable excuse is an offence liable to an unlimited fine.

Payment Practices and Performance Reporting Obligations

Additional narrative reporting obligations came into force in 2017, contained in the Payment Practices and Performance Regulations 2017, requiring large companies to publish specific information about the payment of their suppliers. These regulations are supported by the updated BEIS Guidance published in October 2017. Some companies' reporting deadlines will already have been reached; for companies with a December year end, first submissions are required by 30 July 2018.

Who must report? Large companies and LLPs meeting two or more of the following thresholds:

- £36m annual turnover:
- £18m balance sheet;
- 250 employees.

When must the payment practices report be made? Companies are required to report twice a year on their payment practices. The regulations apply to financial reporting years starting on or after 6 April 2017 and the first report is due within 30 days of the end of the first reporting period for that financial year (see Table A for a breakdown of reporting periods and relevant reporting dates).

Qualifying Contracts

Qualifying Contracts include all contracts (including intragroup contracts), whether verbal or written, for goods, services and intangible property (including IP), which have a significant connection with the UK.

What payment practices and performance information needs to be included? In respect of Qualifying Contracts, large companies and LLPs are required to provide specific information on:

- **Payment terms:** including the payment period specified, any changes to the standard payment terms within the reporting period and a description of the maximum payment period specified in Qualifying Contracts entered into during the reporting period.
- **Dispute resolution:** processes for resolving payment disputes.
- **Payment practices and policies:** processes for making payments and tracking of invoices.
- **Payment performance**: the average time it takes to pay the suppliers from receipt of the invoice and the percentage of payments not made within the payment period.

The report and its contents must be approved by a director of the company and details of the approving person must be provided with the report.

Table A[1]: Reporting deadlines

First reporting period began in 2017:

Financial Year beginning	What is the first reporting period?	When must the first report be published on the web service?
6 April 2017	6 April to 5 October 2017	On or before 4 November 2017
After 6 April 2017	First six months of the business' 2017-2018 financial year	Within 30 days starting on the day after the end of the business' first reporting period.

For those with a financial year end between 31 December 2017 and 4 April 2018 the first reporting period will begin in 2018:

Financial Year beginning	What is the first reporting period?	When must the first report be published on the web service?
1 January 2018	1 January 2018 to 30 June 2018	On or before 30 July 2018
1 April 2018	1 April 2018 to 30 September 2018	On or before 30 October 2018
5 April 2018	5 April 2018 to 4 October 2018	On or before 3 November 2018

1 Paragraph 88, BEIS Guidance

Where must the payment practices report be made available? Businesses can publish their bi-annual reports online via the web-based service provided by the government in the BEIS Guidance.

Sanctions for non-compliance: It is a criminal offence by the business and every director of the company (or designated member of an LLP) if the business fails to publish the correct report within the relevant 30 day period. It is also a criminal offence (by the individual or a business) to publish a report that is misleading, false or deceptive. The offences are punishable by an unlimited fine.

Financial Reporting Council (FRC) changes – Corporate and Financial Reporting

In October 2017 the FRC announced its findings following its Annual Review of Corporate Reporting 2016/2017, which sets out the FRC's assessment of the quality of corporate reporting in the UK, together with its Technical Findings 2016/17. A core message coming out of the review is for companies to ensure that disclosures are specific and detailed, enabling investors to gain a better understanding of the circumstances of a disclosure. Whilst acknowledging that the overall standard of reporting is "generally good", in its advice letter to audit committee chairs and finance directors, the FRC highlighted a number of key areas for additional focus, which include:

- **New accounting standards:** companies were reminded of the importance of clear and qualitative disclosures including analysis of the likely impact of the new accounting standards on their financial statements, with reference to existing accounting policies.
- **Linking different pieces of information:** the letter encourages companies to explain relationships between different pieces of information, for example, between Key Performance Indicators and remuneration policies. Companies are also reminded to ensure that performance disclosures are sufficiently specific, with clear descriptions.
- **Critical judgements and estimates:** investors want to see specific and bespoke explanations of the information given, including how changes to estimates may affect following years' accounting, rather than simple generic disclosures.

Also in October 2017, the FRC's Financial Reporting Lab published an implementation study on how companies have responded to investor calls for better disclosure of dividends, since it published its "Disclosure of dividends – policy and practice report" (**November 2015 Report**).

Disclosure Recommendations
The November 2015 Report contained the following dividend disclosure recommendations for companies:

Dividend policy disclosures should be improved by demonstrating the board's considerations in setting the policy (including risks and constraints), the rationale behind the approach and providing enough detail to explain how the policy will operate in practice; and

Dividend practice disclosures should be improved by including the key judgements and constraints considered in applying the policy and the dividend resources (i.e. setting out distributable profits and reserves).

Editor Comment:

During 2017 we saw various challenges that needed to be addressed by companies to ensure capture of the relevant reporting information. Examples of changes and system updates required include implementing business-wide processes for recording the date of receipt of invoices, implementing systems to gather a comprehensive list of all relevant suppliers and invoices (wherever they are received within the business) and identifying which companies within a group are required to report. It is also vital that companies have thought, in good time, about who will approve the final report and what evidence the approving person will need to see to provide their approval.

The Lab reviewed 313 annual reports published during 2016 and concluded that 132 of those companies have implemented some of the Disclosure Recommendations: 58% of the FTSE 100 made some level of disclosure relating to distributable profits or distributable reserves (up from 40% in 2015 reports), although this figure is only 30% for the FTSE 250. The FRC has again urged companies to adopt its recommendations particularly with respect to reporting on capacity to pay dividends.

BEIS proposes reforms to Corporate Energy and Greenhouse Gas Reporting

In October 2017, BEIS published proposals to streamline the UK corporate energy and carbon reporting framework. The framework has become increasingly complex in the last few years with the introduction of a number of overlapping schemes including the CRC Energy Efficiency Scheme (**CRC**), the Energy Savings Opportunity Scheme (**ESOS**) and Mandatory Greenhouse Gas (**GHG**) reporting. The proposals follow on from the Government's confirmation that the CRC will come to an end in April 2019. The changes are likely to depend on whether relevant companies are quoted or unquoted[2].

For UK quoted companies, BEIS proposes adding energy use to the existing mandatory GHG reporting regime.

New requirements to report on carbon emissions and energy use are proposed for larger unquoted companies registered in the UK and possibly LLPs. Exactly which companies will qualify for the new reporting requirements remains unresolved and BEIS has suggested various different qualification thresholds, including use of the "large companies" concept under the Companies Act 2006.

The proposals float various options for the category which would cover UK electricity, gas and transport energy use, and associated GHG emissions. Qualifying companies would also need to include an intensity ratio tying emissions to quantifiable factors (e.g. turnover or employees). In broad terms, this would be a combination of current CRC reporting and a less onerous version of the GHG reporting requirements applicable to quoted companies. BEIS proposes that all obligated companies should report on opportunities and action, to improve energy efficiency. BEIS is also considering widening the reporting obligations, in particular, whether any elements of the recommendations of the industry-led Task Force on Climate-related Financial Disclosures (**TCFD**) published in June 2017 should become mandatory (see our client briefing).

Reporting will be on a "comply or explain" approach and will be contained in companies' annual reports. The consultation closed at the beginning of January 2018 and BEIS expects the new requirements to be finalised and come into force by April 2019. For more information on these proposals, see our client briefing.

Key Proposals

- Existing framework for mandatory Greenhouse Gas reporting by quoted companies enhanced to include energy use.
- New framework for larger unquoted companies proposed to include mandatory reporting on UK electricity, gas and transport energy use and carbon emissions.
- Reporting extended for all obligated companies to include energy efficiency opportunities and action.
- "Comply or Explain" approach to give some flexibility.
- Reporting within annual reports.

2 As defined in s.385 of the Companies Act 2006

COMPANY LAW UPDATE

Data and Cyber Security Update

In case you missed it… On 25 May 2018, the General Data Protection Regulation (**GDPR**) will become directly effective, without the need for national implementation. Member states are permitted to make limited derogations, which in the UK will take the form of the Data Protection Bill, which repeals the Data Protection Act 1998 and deals with areas such as data processing that falls outside EU law, the EU Law Enforcement Directive, national security and considerations in respect of the UK regulator (the Information Commissioner's Office). The GDPR seeks to modernise the law on data privacy and achieve greater consistency across member states while, at the same time, introducing a raft of new, aggressive and intrusive rules. This is set against the backdrop of businesses across all sectors processing increasing volumes of personal data as part of their day to day operations.

Significantly, the GDPR will bring with it increased reporting and compliance burdens, enhanced rights for data subjects, a broader extra-territorial scope and severe new sanctions. In order to prepare for these changes, businesses are carrying out full data audits and compliance programmes.

How ready are you? Many issues will arise from the GDPR, but focusing attention on key pressure points which strategically affect your business will be important, particularly as May 2018 rapidly approaches. Some of the key action points for businesses include:

- considering whether your business is likely to come within the GDPR's scope;
- undertaking cost and risk analyses for compliance;
- reviewing security arrangements;
- analysing whether a data protection officer will be required;
- reviewing and amending data protection policies to meet the GDPR standards;
- delivering high-level training to key staff involved in the processing of personal data;
- reviewing the organisation's strategy for the justification of its processing of personal data (particularly with regard to consent);
- identifying key existing contracts which will extend significantly beyond May 2018 and involve material outsourced processing of personal data;
- reviewing your approach to international data transfers – including identifying key processes and systems involving restricted intra (or extra-) group international transfers of personal data;
- considering the impact of Brexit in assessing international data transfer strategies;
- analysing requirements (technological, legal and practical) arising in connection with new data subject rights (e.g. maintaining the ability to "port" data to third parties);
- preparing a response package to address exercise of data subject rights; and
- keeping national laws supplementing and creating exceptions to the GDPR under review and, where necessary, devising local compliance strategies.

Editor Comment:

The sanctions regime under the GDPR is far more severe than data protection law of old – from May this year regulators will be entitled to impose fines on breaching organisations of up to 4% of global turnover (or EUR 20 million, whichever is higher).

In the run up to implementation in May, please get in touch with your Clifford Chance contacts should you wish to discuss the impact of the GDPR on your business or how we can assist you. Our teams are currently working with a number of clients to prepare for the GDPR in a range of ways. In particular, we have undertaken the review and implementation of a number of full-scale compliance projects to:

Scope and assess the gap between where the business is now and where it needs to be by May 2018. This involves gathering information about how business units manage individuals' data, and using it to develop a compliance heat-map, illustrating the areas of low, medium and high risk. No two businesses are the same and it is important to ensure a tailored approach to compliance.

Review and refresh processes, policies and systems to meet the requirements of the GDPR. We are working with clients to review and update all relevant policies and agreements, including supplier agreements, data subject notices, privacy policies and consent forms. Where counterparties are involved, clients are seeking guidance as to engagement and negotiation strategies in order to ensure a robust position should a regulator make enquiries further down the line.

GDPR – just the tip of the regulatory iceberg

The GDPR is just one example of heightened regulatory oversight in respect of data and technology. If your business is an operator of critical infrastructure or a digital service provider, new network security obligations are also on the horizon in the form of the EU Security of Network and Information Systems Directive (the **NIS Directive**), which must be transposed into UK law by 9 May 2018.

The NIS Directive will put new obligations on in-scope businesses to ensure that the cybersecurity measures they have in place are appropriate. While it has been left to member states to determine the precise details on a nation-by-nation basis, the UK implementation will likely cover areas such as identity and access control; service protection; data and system security; and staff awareness and training. In addition, firms will face new incident reporting obligations, not only in the context of cybersecurity incidents but also potentially in respect of physical incidents affecting the security of network and information systems. Early indications suggest that the fines for non-compliance in the UK may match those of the GDPR.

Globally new cyber regimes are coming into force, including new regimes in New York and China in 2017 and in Australia later this year. Many clients are keen to address their obligations under the NIS Directive and other cyber regimes at the same time as addressing their GDPR compliance issues.

Update to Modern Slavery Guidelines

The UK's commitment to tackling modern slavery has not waned. The Prime Minister has made clear that businesses should not be knowingly or unknowingly complicit in modern slavery crimes. Indeed, at the UN General Assembly session in September, the Prime Minister announced that the UK would direct £150 million of funding to modern slavery initiatives. In October 2017, two years after the reporting requirement under section 54 of the Modern Slavery Act 2015 (**MSA**) came into effect, the UK government issued updated statutory guidance, which, among other things, highlights to businesses the benefits of producing modern slavery statements, even when they are not strictly required to do so.

Voluntary reporting

The MSA requires that all companies with a turnover of £36 million or more produce a slavery and human trafficking statement for each financial year in which they meet the threshold. A major focus of the revised guidance is to encourage companies that perhaps fall short of this threshold to still report voluntarily and it strongly recommends that organisations continue to report even in years that they do not meet the threshold. The guidance notes the practical benefits of doing so, including building up a consistent approach to modern slavery year on year and the potential benefit for companies to already have, when asked by others in their supply chain, a policy on tackling modern slavery. The guidance further reminds smaller companies of the benefits to them if they find themselves competing for work alongside larger companies which are already required to provide the statement.

Where a company is required to make a statement on modern slavery, the guidance recognises that the areas proposed in section 54(5) of the MSA remain optional (including policies, due diligence, risk exposure and effectiveness at tackling modern slavery), but stipulates that the relevant organisation should aim to include information covering those areas and "paint a detailed picture" of all the steps it has taken both to address and remedy modern slavery as well as an assessment of the effectiveness of those steps.

Organisations are encouraged to report as soon as possible after their financial year end and should ensure that they keep statements from previous years available on their websites as well.

Criminal Finances Act 2017 – corporate offences of failure to prevent the criminal facilitation of tax evasion

In our last Corporate Update we detailed the new requirements of the Criminal Finances Act 2017, which brought into force the corporate offences of failure to prevent facilitation of tax evasion on 30 September 2017. Also in September 2017, HMRC published guidance containing the procedures that relevant bodies can put in place to prevent persons associated with them from committing tax evasion facilitation offences.

Given the scope of the offences, which are highly extra-territorial and apply to both companies and partnerships not only in the UK, but worldwide, and can be triggered by the evasion of non-UK taxes, it is crucial that businesses have appropriately updated policies and procedures. The only defence is for a company to be able to show that it had reasonable prevention procedures in place at the time of the offence or that it was not reasonable in all circumstances for it to have such prevention procedures in place.

Editor Comment:

Exactly what is necessary for each business to implement will vary from business to business, but the key elements that need to be in place are a demonstration of top level commitment from within the business, accompanied by a message from management to all employees; a detailed risk assessment; amendments to the internal code of conduct; training; and ongoing monitoring and review. We have worked with numerous clients (ranging from multinational banks and energy companies to UK domestic retailers) to carry out risk assessments and to ensure there are suitable procedures in place to manage the risks for that business. We are also starting to see this issue raised by buyers in corporate transactions and by underwriters' counsel in capital market transactions. Our tax and white collar crime group are well placed to help clients in relation to the relevant issues.

REGULATORY UPDATE

Notification obligations under MAR where director holds multiple directorships

The City of London Law Society and Law Society Company Law Committee Joint Working Group has updated its MAR Q&A guidance in relation to the notification obligations of companies with directors holding multiple directorships. The update follows the revision by ESMA in July 2017 of its MAR Q&A on this point.

PDMR notification obligations: By way of reminder, under MAR, a person discharging managerial responsibility (**PDMR**) of an issuer, such as a director, and his or her "persons closely associated" (**PCA**s) must notify the issuer and the FCA of every transaction conducted on their own account relating to the shares or debt instruments of the issuer or other financial instruments relating to such shares or debt instruments (Art 19 MAR). The definition of PCA is set out in Art 3(1)(26) MAR and includes legal persons (i.e. companies), the managerial responsibilities of which are discharged by a PDMR (or its PCA), who is directly or indirectly controlled by such a person.

PDMR with multiple directorships: The previously held view was that that where a person is a director of both company A and company B, in circumstances where company B dealt in the shares of company A, company B was not treated as a PCA of the director (which would require company B to notify company A and the FCA of its dealing) so long as he or she was not the sole director of company B or otherwise controlled B's management decisions. As there is no definition of "control" in MAR, this phrase should be given its ordinary meaning, that is, control of a majority of the voting rights of the company in question. As such, if the director owned 60% of the shares in company B, this would make company B a PCA of the director, even if the director did not take part in or influence any decision of company B to carry out a transaction in the financial instruments of company A.

However, under the ESMA Q&A published in July 2017, the position has been altered. Company B will be treated as a PCA of a director, simply by virtue of the individual being a PDMR of company B. As such, were company B to deal in company A's financial instruments, company B would need to notify company A and the FCA of any such dealing.

The Joint Working Group's Q&A clarifies this change in practice and offers some practical advice to market participants to assist them in avoiding this situation arising. In particular, company B will not be treated as a PCA of the director under the example above unless and until company B carries out a transaction in company A's financial instruments. In addition, if company B does carry out a transaction in the financial instruments of company A, company B will only be treated as a PCA if the director took part in or influenced the decision of company B to carry out that transaction. In order to avoid making company B a PCA, the director should not vote on, participate in any discussion in relation to, or otherwise influence any decision of company B to carry out, a transaction in the financial instruments of company A. It will be sufficient in this regard that the director recuse him/herself from any board meeting discussing or relating to company A, unless on the specific facts of the case the director otherwise exerted an influence on company B's decision. Company A need not include company B on its list of PCAs, and the director should not notify company B in writing of its obligations as a PCA unless and until company B carries out a transaction in the securities of company A and the director participated in or influenced company B's decision to do so.

Separately, companies should remember that there is a separate regime for significant shareholders (holding over 3% of the share capital of an issuer and any changes above that amount through a whole percentage point) to notify such holdings to an issuer and the market (see DTR 5 of the FCA's Disclosure and Transparency Rules).

Editor Comment:

Given this change in practice, it would be advisable for directors holding cross directorships to be reminded of their obligations in this regard and to ensure that, where possible, they recuse themselves from any decision making by the company to deal in the securities of another company in relation to which they hold a board position.

FCA enforcement actions

The latter half of 2017 was busy for the FCA and we saw a number of final notices issued against both individuals and companies. We highlight below the most significant of these and in particular, consider the first enforcement action taken by the FCA under Article 17 MAR.

FCA fines company £70,000 for failure to disclose inside information (Article 17 MAR)

On 14 December 2017 the FCA issued a final notice imposing a fine of £70,000 on Tejoori Limited, an AIM listed company (since de-listed), for failure to disclose inside information between 12 July 2016 and 23 August 2016. This is the first fine imposed by the FCA under Article 17 MAR.

Tejoori is a closed-ended investment company with total investments of USD 17.26 million. On 28 July 2016 Tejoori agreed to sell one of its investments, a minority holding in a private German renewable energy company, BEKON, to another private company, Eggersmann, as a consequence of major shareholders in BEKON exercising drag-along rights. The shares were transferred on 10 August 2016.

Tejoori had ascribed a value of USD 3.35m to its investment in BEKON. The consideration received by Tejoori as part of the drag-along transaction was considerably lower than USD3.35m. Tejoori did not make any announcement when entering into the transaction (in part because its Board did not fully understand the deferred consideration and therefore did not understand that the consideration to be received was lower than the value ascribed in the accounts). Both BEKON and Eggersmann publicised the transaction but were not required to disclose the terms as both are private companies. After that publicity, Tejoori's share price rose significantly as a result of speculation in the market as to what consideration it had received.
On 24 August 2016 Tejoori made an announcement explaining the terms of the transaction, following which, its share price fell.

How is inside information identified? The FCA considered two elements of the 'inside information' test; when information is 'precise' and whether it will have a 'significant effect' on the price of the securities.

Precise: The FCA found that Tejoori had precise information from 12 July 2016 when it had received from BEKON a draft drag-along notice, a draft SPA and a spreadsheet setting out the consideration Tejoori would receive. In the FCA's view this gave rise to a reasonable expectation that Tejoori would be required sell its BEKON shares for consideration significantly less than Tejoori's valuation of its investment in BEKON. It is noteworthy that Tejoori had been aware of the proposed terms of the transaction from 8 June 2016, and knew that majority shareholders were likely to exercise drag-along rights from 29 June 2016. It may be that there was some negotiation between Tejoori and the FCA before settlement as to when the information regarding the transaction was sufficiently precise. The FCA's findings on this issue may have been influenced by the fact that MAR did not come into effect until 3 July 2016.

Significant effect: The FCA considered that this information was likely to have a significant effect on Tejoori's share price on the basis that "*a substantial diminution in the value of a significant investment is information of a kind which a reasonable investor would be likely to use as part of the basis of their investment decisions due to the fact that it would likely cause a decrease in Tejoori's share price*". Interestingly Tejoori's share price appears to have been higher after the announcement explaining the terms of the transaction (0.7789 close on 24 August) than it had been when the inside information is said to have arisen (0.7753 close on 12 July). This issue is not dealt with by the FCA in the notice.

Penalty: As is normal in disclosure cases, the FCA calculated the fine by taking a percentage of the firm's average market capitalisation during the period of the false market. The percentage used varies depending on the seriousness of the case. The FCA's starting point for the penalty was 0.125% of Tejoori's average market capitalisation between 12 July 2016 and 24 August 2016, which was £6,893,716. The FCA considered that the figure this produced was too low to deter others from the same conduct and so increased the penalty to £100,000 which figure was then reduced to £70,000 on early settlement.

Inside Information:

- information of a precise nature:
- which has not been made public;
- relating, directly or indirectly, to one or more issuers or to one or more financial instruments; and
- if it were made public, would be likely to have a significant effect on the prices of those financial instruments or on the price of related derivative financial instruments (information that a reasonable investor would be likely to use as part of the basis of their investment decisions).

(*Article 7(1)(a) and 7(4), MAR*).

FCA fines ex trader £60,090 for engaging in market abuse

On 22 November 2017 the FCA published a final notice imposing a fine of £60,090 on a former bond trader for engaging in market abuse.

Following an investigation, the FCA found that the individual, an experienced trader, had engaged in market abuse by "*creating a false and misleading impression*" as to supply and demand in the market for Dutch state loans on 12 occasions over the period from 2 July to 8 August 2014. He did this by entering quotes on the relevant trading platform that were designed to induce other market participants tracking activity to raise or lower their quotes so that he could benefit from those price movements.

Even though he was found to have *negligently* rather than *deliberately* committed market abuse, the FCA still held this as a serious example of market abuse, citing that as a trader with 20 years of experience and as an approved person, the trader should have realised that his behaviour amounted to market abuse and a failure to act in accordance with standards reasonably expected of market participants.

Penalty: In arriving at the amount of the fine to be imposed, the FCA found that the individual had not personally derived any financial benefit from the market abuse and because the market abuse was referable to his employment, the fine was based on a percentage of his earnings in the 12 months prior to the market abuse activities.

FCA fines company £27,385,400 for breach of Disclosure and Transparency Rules

On 17 October 2017 the FCA announced that it has fined Rio Tinto plc £27,385,400 for breaching the DTRs. The FCA found that Rio Tinto breached DTR 1.3.4R and DTR 4.2.4R(1) by failing to carry out an impairment test and to recognise an impairment loss on the value of mining assets based in the Republic of Mozambique (which it acquired in August 2011 for US$3.7 billion) when publishing its 2012 interim results on 8 August 2012.

Penalty: In arriving at the amount of the fine to be imposed, the FCA found that the company had not derived any financial benefit from the breach, so there was no amount to be subject to disgorgement. The FCA found the seriousness of this offence to be Level 2, the lowest level which can produce a financial penalty, so its starting point for the penalty was 0.125% of Rio Tinto's average market capitalisation over the period of the breaches (29 May 2012 – 8 August 2012). The FCA considered that this resulted in a figure that was disproportionately high and it was therefore reduced by 25%. The total penalty was reduced by a further 30% for agreeing to settle at an early stage.

NEW FOREIGN INVESTMENT PROPOSALS

UK reviews national security impact of foreign investment

On 17 October 2017, the UK Government published a green paper setting out proposals for new measures in the short term for companies that design or manufacture military and dual use products, and parts of the advanced technology and longer term proposals for the creation of a new, standalone regime to vet national security issues in a range of foreign investments.

The green paper for the first time identifies the national security concerns which the Government considers may arise from foreign ownership or control of critical national infrastructure or advanced technology companies, as follows:

- increased access (to businesses, physical assets, people, operations or data) and ability to undertake espionage;
- greater opportunity to undertake disruptive or destructive actions or an increase in the impact of such actions; and
- the ability to exploit an investment to dictate or alter services or to utilise ownership or control as inappropriate leverage in other negotiations.

The Short Term Proposals

The Government already has powers to intervene in mergers that may give rise to national security concerns, under the Enterprise Act 2002, which also establishes the UK's merger control regime. However, it can only do so where the transaction meets the turnover thresholds under the EU Merger Regulation or the turnover or share of supply thresholds of the UK merger regime, or where the target is a Government defence contractor. The short term proposals set out in the green paper seek to bring transactions within the scope of the Government's power to intervene on national security grounds if they meet much lower thresholds than apply under the current EU and UK merger control regimes, i.e. where the target business:

- has turnover of over £1 million or a market share of 25% or more in any UK market; and
- is active in either: (i) the military and dual use sector (i.e. it designs or manufactures items, or holds related software and technology, specified on the UK Military List, UK Dual-Use List, UK Radioactive Source List and EU Dual-Use Lists); or (ii) certain activities in the advanced technology sector relating to intellectual property rights in the "functional capability of multi-purpose computing hardware", "roots of trust" of such hardware, or quantum computing / communications technologies.

The short term reforms would give the Government the power to call in mergers meeting these new, lower thresholds for review on national security grounds and to impose appropriate remedies where national security concerns are identified. However, they would not create any mandatory filing obligations.

The green paper states that the Government intends to "press ahead with the specific amendments needed immediately after consultation", which will be done by secondary

Emerging Government Thinking

The UK Government has published proposals to strengthen its powers to review, and potentially block or unwind, investments on national security grounds. Short term proposals include amending the thresholds of the existing public interest regime to catch a broader range of investments in the military and dual use sector and the advanced technology sector. These could affect transactions that are currently under contemplation. In the longer term, the Government is considering the introduction of a more extensive regime for screening transactions for national security issues. Options include powers to "call in" a wide range of foreign investments (including new projects and acquisitions of bare assets) for screening and/or a mandatory notification regime for foreign investment in certain key sectors such as nuclear, defence, energy, transport and telecoms.

legislation, so transactions currently being planned could be affected. While the green paper stresses that the Government's objectives in amending the thresholds relate solely to dealing with national security-related issues, the proposed use of secondary legislation means that such transactions will nevertheless be subjected to a review on competition grounds, in addition to the national security vetting process.

Options for Long Term Reform

In the longer term, the Government is considering two options for the introduction of a more comprehensive regime for screening foreign investments, which could be implemented alone or in combination: (a) an expanded version of the voluntary filing regime under the Enterprise Act 2002; and/or (b) a mandatory notification regime for foreign investment in businesses performing certain "essential functions". Detailed proposals will be set out in a white paper to be published later this year.

(a) Expanded voluntary regime

Under this option, the Secretary of State would be able to make a special "national security intervention" in respect of a broader range of transactions than is currently possible under the Enterprise Act, including the following:

- Acquisitions of "significant influence or control" over a UK business entity, which the Government is minded to define as the acquisition of either: (i) more than 25% of a company's shares or votes; or (ii) less than 25%, but with other means of exercising such control, to be clarified in Government guidance.
- New projects, in particular, developments and other business activities that are not yet functioning businesses but can reasonably be expected to have future activities that may affect national security interests.
- Sales of bare assets (i.e. assets such as machinery or intellectual property transferred without the other elements of a stand-alone business) or land in proximity to a sensitive Government site.

If not voluntarily notified, such transactions could be "called in" for review by the Secretary of State within a certain period (envisaged to be three months) if he or she believes that the transaction raises national security risks. The national security review would be a separate process to any review on competition or other public interest grounds. The green paper does not appear to envisage any turnover or market share thresholds, such that a very wide range of transactions would become potentially reviewable.

(b) Mandatory filing regime

Under this option, there would be a mandatory filing requirement for acquisitions by foreign investors of significant influence or control (as described above) over businesses with certain "essential functions" in the following sectors: civil nuclear, communications, advanced technology, defence, energy, transport, emergency services and government services. Acquisitions of land in proximity to a national security-sensitive site would also be notifiable. The Government would have the power to specify individual businesses or assets not active in the above areas for inclusion in the mandatory screening regime, e.g. where they supply critical goods/ services to national infrastructure firms.

The green paper does not appear to envisage any turnover or market share thresholds: if the target operates or provides infrastructure, goods or services that meet the relevant criteria, any foreign investment conferring significant influence or control would be notifiable. Standstill obligations would apply to prevent completion or implementation of such a transaction prior to Government clearance, with civil and/or criminal penalties for breach of such obligations. The green paper does not indicate how long the screening process would take, other than to indicate that most transactions would be expected to receive rapid approval.

Editor Comment:

The green paper emphasises that the Government intends for the UK to remain amongst the most open economies to foreign investment and that its proposals have been designed with the sole aim of addressing legitimate national security concerns. This focus on defined national security issues, coupled with the possibility of judicial review of decisions to block, unwind or impose remedies on a transaction, suggests that the regime should not become a Trojan Horse for other considerations to be taken into account, such as protectionism of national champions or a merger's impact on employment.

The green paper also emphasises the Government's intention to implement only those reforms that are necessary and proportionate to protect national security. However, it is questionable whether a mandatory filing regime would be consistent with that aim. Mandatory notification would impose filing burdens on a relatively large number of transactions, the great majority of which would (as the green paper acknowledges) pose no national security issues at all. The Government estimates that a mandatory regime would catch up to 100 transactions per year: almost double the number of transactions per year that are reviewed on competition grounds under the voluntary merger control regime.

EU Proposal for Screening of Foreign Direct Investments

The European Commission has presented proposed legislation that would create an EU framework for screening of foreign takeovers and investments on grounds of security and public policy. The draft Regulation would allow the Commission to review (but not block) certain investments of "Union interest" and to issue a non-binding opinion to the member state in which the investment takes place. It would also clarify the scope of the issues that member states may take into account when applying their national screening regimes without falling foul of EU law, set certain common standards for those regimes and implement a system of cooperation and information exchange between member states and the Commission. While the legislation is unlikely to come into force before the UK leaves the EU in March 2019, it might nonetheless be applicable in the UK if there is a transitional period following Brexit within which the UK agrees to adopt new EU legislation. For more information, see our September 2017 client briefing.

CASE LAW UPDATE

Can a company ignore a request for a copy of its register of members from an asset tracing business?

Companies are required by law to keep a register of members which contains the names and addresses of the shareholders and the number of shares held by them. Any person may inspect and take copies of the register of members on the payment of a fee. Any request to inspect and/or take copies must contain the information required by law, which includes the purpose for which the information is to be used. Where a company receives such a request, it must within five working days either comply with the request or apply to the court. If an application to the court is made, the court can direct the company not to comply with the request if it is satisfied that the request is not sought for a **proper purpose**.

In 2013, Burberry Plc received such a request from an individual, Richard Charles Fox-Davies, who owned an asset tracing business. Burberry made an application to the court, which held that the request was not for a proper purpose. Mr. Fox-Davies appealed this decision and so in July 2017 the Court of Appeal had to decide whether his purpose in requesting a copy of the register was a proper purpose.[3]

Is asset tracing a proper purpose? Proper purpose has been intentionally left undefined so it is up to the courts to determine proper and improper purposes on a case by case basis. Whether a purpose is proper will often depend on the precise facts and circumstances. It appears from the Court of Appeal's decision in the Burberry case that asset tracing for commercial gain in itself is not an improper purpose, however, the terms on which the tracing activity is carried out may render the asset tracing an improper purpose.

In the Burberry case, the court refused access to the register. Refusal was based on either (i) the request being improper because of the practice of extracting a commission from traced lost shareholders by not disclosing the asset to which they may be entitled before they agreed to pay Mr Fox-Davies' commission or (ii) the fact that the court could not properly determine whether or not the purpose was proper because the court was not given any information about the commercial charges for re-connecting lost shareholders with Burberry. If the terms on which a lost shareholder may be re-connected to the company are commercially oppressive, a court can find that the purpose is improper.

Editor Comment:

If a company receives a request from an asset tracing business to inspect and/or take copies of its register of members, this request should not be ignored. If the asset tracing business has sent a request that contains all the information required by law and is transparent about the fees it charges to lost shareholders, then it may be difficult for a company to refuse such a request.

3 Richard Charles Fox-Davies v Burberry Plc [2017] EWCA Civ 1129

Can "to the extent" mean "if"?

According to obiter comments in a recent case[4], the words "to the extent" are capable of meaning "if" and such a meaning is a natural meaning of those words. The case concerned a limitation on liability in a share purchase agreement that a seller would not be liable for any warranty claim to the extent that provision or reserve in respect of the liability was made in the accounts. In this case, where the Court gave weight to the commercial position, this limitation meant that if there was a provision in the accounts (regardless of the sufficiency of the provisions), there would be no liability for a seller at all (rather than a seller having no liability up to the amount of the provision but being liable for any amount over and above the provision).

Editor Comment:

Many practitioners have been surprised by this obiter comment, however, in light of it, would be prudent, where any commercial agreements use the term "to the extent", to consider whether the drafting could be made clearer.

4 Zayo Group International Limited v Michael Ainger and others [2017] EWHC 2542 (Comm)

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This Corporate Update has been produced by the London Corporate Practice and edited by Nicholas Rees.

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J2018 01160052088