

FCA consultation on a new category of premium listing for sovereign controlled companies

July 24, 2017

Introduction

On July 13, 2017, the UK Financial Conduct Authority (the “**FCA**”) published a consultation paper entitled “*Proposal to create a new premium listing category for sovereign controlled companies*” (“**CP 17/21**”), which recommends some targeted amendments to the UK Listing Rules to make the UK capital markets more accessible to companies which are directly or indirectly controlled by a nation state.

The FCA has asked for responses to the questions raised in the consultation paper by October 13, 2017, and intends to publish the final rules in a policy statement before the end of 2017. This memorandum sets out the key proposals of CP 17/21 and provides some considerations as to how the new regime, if implemented, may work in practice.

Background

The listing regime for the UK’s Official List is divided into the premium and standard listing segments. The requirements for a standard listing stem from the relevant EU directives and regulations that apply to regulated markets across the EU. For admittance to the premium listing segment, a company is required to meet higher UK specific standards that are intended to provide additional investor protection and promote shareholder confidence.

The premium listing segment is currently available only for listings of equity shares by commercial companies, closed-ended investment funds, and open-ended investment companies.

CP 17/21 envisages the creation of a fourth category of the premium listing segment exclusively for sovereign controlled companies. Whilst the FCA does not anticipate that many companies will list under this new category, it is their view that it will attract companies which, under the current regime, would be deterred from listing in London on account of restrictions to relationships between large shareholders and listed entities (CP 17/21, paragraph 3.5).

The FCA is of the opinion that sovereign controlled companies should receive dispensations from the UK Listing Rules that apply to commercial companies with premium listings who have large private sector shareholders. This is because sovereign owners tend to be different from private sector owners in both their motivations and nature, and investors who choose to invest in sovereign controlled companies do so after taking account of the sovereign owner (CP 17/21, paragraphs 3.4 and 3.7).

It could be argued that the proposed new category will provide investors with greater protection, as sovereign controlled companies with premium listings will be required to meet higher standards than if their securities were admitted to the standard listing segment.

FTSE UK Index Series inclusion

Only companies with equity shares listed on the premium listing segment are eligible to be included on the FTSE UK Index Series. The FCA is not responsible for the FTSE UK Index Series and, therefore, whilst CP 17/21 provides sovereign controlled companies with easier access to the premium listing segment, the FCA acknowledges that many of the companies that would be eligible for the new category

would not, under the current **FTSE Ground Rules** (the “**Ground Rules**”), meet the eligibility requirements of the FTSE UK Index Series (CP 17/21, paragraph 3.25).

Not gaining access to the FTSE UK Index Series may well deter companies from seeking this new premium listing. It remains to be seen whether FTSE will follow the FCA’s example and look to amend the Ground Rules to accommodate sovereign controlled companies. In particular, for most sovereign controlled companies, the biggest hurdle to FTSE UK index inclusion will be the free float requirement under the Ground Rules. Assuming a company is not adjudged to have UK nationality, it would currently require a 50% free float to be eligible for inclusion.

Eligibility for the new category

Sovereign controlling shareholder

In order to qualify for the new category, a commercial company must have a “**sovereign controlling shareholder**”, which means a shareholder:

- who is a sovereign or other head of state acting in his or her public capacity or a government or a department, agency or special purpose vehicle of that government; and
- who exercises or controls 30% or more of the votes to be cast on all or substantially all matters at general meetings of that company (CP 17/21, Appendix 1, page 3).

The definition is broadly the same as for a controlling shareholder under the existing UK Listing Rules (see “Controlling shareholders” below), but note that a sovereign controlling shareholder cannot aggregate any interests held by parties acting in concert, which are relevant for determining the size of any other controlling shareholder’s interest.

Existing companies with a sovereign controlling shareholder will be eligible to transfer into the new category provided approval is received from shareholders, which will involve a vote of all shareholders requiring not less than 75% of the shares voted on the resolution, and another vote excluding any sovereign controlling shareholders and any other controlling shareholders requiring a majority of shares voted on the resolution (CP 17/21, Appendix 1, pages 13 and 14).

Shares or depositary receipts

As well as equity shares, the FCA’s proposals will allow depositary receipts over equity shares to be listed within the new category (CP 17/21, paragraphs 3.44 to 3.52). This is not currently the case for the other categories of the premium listing segment and CP 17/21 does not seek to change this.

Where depositary receipts are listed by a sovereign controlled company, all shareholder rights will have to pass straight through to the depositary receipt holder such that depositary receipt holders will be treated as if they are shareholders for the purposes of the protections afforded to shareholders under the UK premium listing regime.

For the avoidance of doubt, it will be the company and no other entity that will issue the depositary receipts in order to be eligible for the new category. The company will be required to appoint a sponsor for the purposes of the listing, and whilst a prospectus for depositary receipts does not require the inclusion of a working capital statement, CP 17/21 states that if the company does not include the statement in the prospectus, it will have to be included on the company’s website.

Controlling shareholders

For a commercial company to qualify for the premium listing segment, it must ensure that it can remain independent of any “**controlling shareholder**”. A controlling shareholder is broadly a person who exercises or controls on their own, or together with any person with whom they are acting in concert, 30% or more of the votes able to be cast on all or substantially all matters at a general meeting of the company (LR 6.1.2A R)).

To achieve this, the UK Listing Rules require that:

- a company enters into a relationship agreement with a controlling shareholder, which includes prescribed provisions that ensure the company’s independence and compliance with the UK listing regime (LR 6.1.4B(1) R and LR 6.1.4D R); and
- a company’s constitution must allow for independent directors to be elected and re-elected by a vote of all shareholders other than any controlling shareholders (LR 6.1.4B(2) R).

Under the FCA proposals, these requirements would not apply to a sovereign controlling shareholder, but would apply to any other controlling shareholder of that company. To mitigate any concern that investors will not be appropriately protected, the FCA notes that the following safeguards will remain in place:

- any cancellation of listing or transfer to a standard listing would require the approval of shareholders or depositary receipt holders, excluding any sovereign controlling shareholders or other controlling shareholders (CP 17/21, paragraph 3.43);
- the guidance as to whether a company is complying with its ongoing obligation to remain an independent business will explicitly state that the grant of security over its business in connection with the funding of the sovereign controlling shareholder may indicate that the company does not satisfy its eligibility for listing requirements (CP 17/21, paragraphs 3.28 and 3.29); and
- under section 75(5) of the Financial Services and Markets Act 2000 (the “**FSMA**”), the FCA has an overarching power to reject any application for listing where it would be detrimental to investors. As such, even if a sovereign controlled company met all the UK listing requirements, the FCA will still have the power to deny the listing (CP 17/21, paragraph 3.41).

Related parties

The premium listing regime imposes certain controls on commercial companies entering into a transaction with a “**related party**”, which includes any shareholder of the company who is entitled to exercise, or to control, 10% or more of the votes to be cast on all or substantially all matters at a general meeting of the company.

These controls include:

- for larger transactions, where one of the ratios relating to the gross assets, profits, consideration or gross capital of the company and the target is at least 5%, the company must seek shareholder approval from all shareholders other than the related party (LR 11.1.7 R to LR 11.1.9 R); and
- for smaller transactions, where all of those ratios are less than 5% but one exceeds 0.25%, the company must announce such transaction and have an investment bank, acting as the company’s sponsor, confirm that the terms of the transaction are fair and reasonable as far as the shareholders of the company are concerned (LR 11.1.10 R).

The FCA proposes that a sovereign controlling shareholder will not be a related party to a company with a premium listing under the new category. Instead, investors will receive sufficient protection in respect of related party-type transactions from the requirements on the company:

- under the Market Abuse Regulation (596/2014) (“**MAR**”), to announce all price sensitive information, the inference being that any large transaction will be required to be announced on the basis that it would have a significant effect on the company's share price (CP 17/21, paragraph 3.37); and
- under the UK Listing Rules:
 - to announce any transactions that would have required a shareholder vote under the related party transaction regime (i.e. where one of the ratios explained above is at least 5%);
 - to seek shareholder approval for very large transactions with the sovereign controlling shareholder (i.e. where one of the ratios explained above is at least 25%), albeit any sovereign controlling shareholder would be able to vote on such resolution; and
 - to announce related party transactions as part of its financial reporting under the requirements of international accounting standards (CP 17/21, paragraph 3.37).

Remaining eligibility requirements and ongoing obligations

Other than as set out above, the rest of the UK Listing Rules, UK Disclosure Guidance and Transparency Rules and MAR will apply to a sovereign controlled company with a premium listing. This means that, in order to list, a company will, amongst other things, need:

- a three-year financial history (LR 6.1.3 R);
- an ability to demonstrate that it will be carrying on an independent business as its main activity (LR 6.1.4 R);
- an unqualified working capital statement (LR 6.1.16 R); and
- sufficient securities to be placed in public hands (LR 6.1.19 R).

Once its shares or depositary receipts are admitted to listing, the company will need to retain its free float and independence and also comply in full with, amongst other things:

- the requirements for periodic financial reporting (DTR 4 and LR 9.7A and 9.8);
- the vote holder and issuer notification rules (DTR 5);
- the requirement to make a corporate governance statement (DTR 7.2);
- the disclosure of inside information (MAR, Article 17); and
- the disclosure of dealings by persons discharging managerial responsibility (MAR, Article 19).

Exiting the new category

Where a company listed on the new category of the premium listing segment no longer has a sovereign controlling shareholder, it will be required to move its listing to the commercial company category on the premium listing segment or to the standard listing segment or otherwise delist (CP 17/21, paragraphs 3.53 to 3.57).

If the company chooses not to list on the premium listing segment, this will require a shareholder vote which will exclude all non-independent shareholders.

If the company has listed depositary receipts, it will be required to move to the standard listing segment or delist as depositary receipts cannot currently be listed on the premium listing segment other than in the sovereign controlled company category.

If you have any questions regarding the matters covered in this publication, please contact any of the lawyers listed below or your regular Davis Polk contact.

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