Victoria Richardson
Primary Market Policy
Financial Services Authority
25 The North Colonnade
Canary Wharf
London E14 5HS

By email to: cp12_25@fsa.gov.uk

2 January 2013

NAPF RESPONSE TO CP12/25 – ENHANCING THE EFFECTIVENESS OF THE LISTING REGIME

The NAPF

The NAPF is the leading voice of workplace pensions in the UK. We speak for 1,300 pension schemes with some 16 million members and assets of around £900 billion. NAPF members also include over 400 businesses providing essential services to the pensions sector.

Executive summary

The NAPF welcomes the opportunity to respond to the FSA's consultation 'enhancing the effectiveness of the listing regime'. We believe that plans to bolster the corporate governance aspect of the listing rules are important and welcome.

We believe that the proposals with regard to new arrangements for companies with a controlling shareholder are positive and have the potential to provide significantly greater protection for independent shareholders. These proposals may allay some of the concerns that have been expressed in relation to some of the recent entries to the UK Premium market which have caused consternation amongst investors. Elements such as the requirement for majority independent boards and relationship agreements which need to be continually adhered to are positive. Clarity is however, needed with regards to the sanctions which would be imposed on a company which breached these proposals - a possible sanction should be a transfer from Premium to Standard listing.

We do have concerns with regards to the dual voting structure as it is currently proposed and we also continue to believe that liquidity considerations alone should not determine the free float threshold. As set out in the Kay report, there is increasing attention being given to the role of shareholders in improving long term corporate performance; a greater free float would be helpful in this respect.

In order to respond to the concerns expressed, largely from sell side market participants, that steps need to be taken to increase the attractiveness of our listing regime to growing companies, the FSA is right to look at increasing the flexibility of entry to the Standard segment. We believe that this route should be further promoted and those companies wishing to list with less than a 25% free float should be encouraged to explore this avenue.

A reputation for high standards of governance, transparency and protection of minority shareholder rights is, in our view, vital to maintaining the reputation, integrity and thus attractiveness of the UK market for both investors and issuers. Therefore the development and promotion of the Standard segment should be a priority, ensuring that there is a natural and appealing home for less mature fast-growing companies wishing to list in London whilst protecting the reputation and integrity of the Premium segment.

David Paterson
Head of Corporate Governance
NAPF

CONSULTATION QUESTIONS

Independent business

Independent business and controlling shareholders

Q1: Do you agree with our definitions of a controlling shareholder and an associate of a controlling shareholder? Do you believe that there are other criteria where an entity or a person ought to be deemed controlling shareholder that have not been captured by the proposed definition and if so what are they?

We agree with the proposed definitions of a controlling shareholder (which is consistent with the definition of "control" under the UK Takeover Code) and an associate of a controlling shareholder.

Relationship agreements

Q2: Do you support our proposal in LR 6.1.4ER (1) to require new applicants where a controlling shareholder is present to enter into a relationship agreement?

We welcome the proposal to reinstate the requirement for a relationship agreement to be in place where a controlling shareholder is present. This is a positive move and reinforces the best practice which occurs in most such instances at present.

In addition, we believe that a relationship agreement would be useful in situations where a company has a 'block holder' (e.g. a holder of 25% of the issued share capital, a stake sufficient in the UK to block a special resolution at a shareholder meetings) or a shareholder whose stake in the company gives them a right to appoint a representative to the company's board.

Q3: Do you support our proposal in LR 6.1.4FR to require that a relationship agreement must cover certain provisions as described above? Do you think that there are any other provisions that should be considered and if so what are they?

We support the stipulation of certain provisions which would be required to be included within relationship agreements. Other provisions that should be considered include:

- Disclosure of any entitlement to board representation;

- A controlling shareholder should abstain from doing anything that would weaken protection of minority shareholder rights through company by-laws/articles of association.

Application on a continuing basis

Q4: Do you agree with our proposal in LR 9.2.2AR (1) that where a company has a controlling shareholder it must have in place a relationship agreement at all times?

Q5: Do you support our proposal to subject a listed company to a continuing obligation to comply with a relationship agreement at all times (LR 9.2.2GR)?

Q6: Do you support our proposal that a listed company must at all times comply with the content requirements for a relationship agreement as set out in LR 6.1.4FR, where applicable (LR 9.2.2AR (1))?

Yes a company with a controlling shareholder should be required to enter into a relationship agreement and be required to continue to comply with this agreement at all times. This proposal will potentially address one frustration with current relationship agreements, namely enforcement, as these proposals will provide the FSA with enforcement powers.

However, it remains unclear what sanctions would be imposed upon a company which breached its relationship agreement. We believe that in order to ensure these agreements are treated with the appropriate level of seriousness, a potential sanction for breach of an agreement should be to transfer the company from a Premium listing to a Standard listing.

Given that it appears the UKLA will be primarily relying on issuers and sponsors for notifications of breaches, it may be appropriate to create a formal channel for investors and other stakeholders to report such breaches to the UKLA or request investigation into suspected breaches.

Amendments to the relationship agreement

Q7: Do you support our proposal to subject material changes to the relationship agreement to an independent shareholder vote (LR 9.2.2CR)?

Yes we agree.

Q8: Do you support our guidance on the factors that the listed company should have regard to in determining whether a change to the relationship agreement is material (LR 9.2.2DG)?

While we agree with this proposal in principal, we do have concerns that the interpretation of materiality can be open to abuse. We would urge the FSA to ensure that this is closely monitored. If shareholders feel that companies are not acting in appropriate good faith in this regard then the FSA should be in a position to swiftly introduce a mandatory requirement that all changes to relationship agreements are subject to independent shareholder approval. It would be unlikely that relationship agreements would be likely to undergo frequent changes as such it could be argued that seeking shareholder approval for all changes is not likely to be unduly onerous for listed companies.

Q9: Do you support our proposal to require a listed company to disclose the current relationship agreement in the annual report (LR 9.8.4R (15))?

Yes.

Independent shareholders

Q10: Do you agree with our definition of an independent shareholder?

Yes this seems sensible, however, as per our response to Q2 we would encourage the FSA to give consideration to the status of so called 'block holders' or a shareholder whose stake in the company gives them a right to appoint a representative to the company's board or other additional rights.

Annual report disclosure

Q11: Do you agree with our proposals to amend LR 9.8.4R to include an obligation to make a statement on the compliance of the listed company with the relationship agreement (LR 9.8.4R (14)) as described above?

We believe that the principal of this proposal is positive; however, in order to strengthen the robustness of the relationship agreement and increase the link to the independent shareholders, we believe that this statement should be signed off by the Senior Independent Director (SID).

Independence in other circumstances

Q12: Do you agree that the proposed guidance (LR 6.1.4DG) contains the key factors indicating that the new applicant may not carry on an independent business? Do you think that there are any other factors that should be considered and if so what are they?

Yes we agree with the suggested factors.

Control of business

Eligibility requirement

Q13: Do you agree with the proposal to amend the requirement for control of assets to control of business (LR 6.1.4AR)?

Yes. We agree that this change reflects a more holistic view of the nature of an issuer's business rather than a more narrow focus on the valuation of assets.

Purpose of control and situations where it may not exist

Q14: Do you agree with the proposed guidance (LR 6.1.4BG) regarding control of business? Do you think that there are any other indicators that should be considered and if so what are they?

Yes the proposed guidance appears sensible.

Application where changes of control occur

Q15: Do you agree with our proposal to supplement guidance in LR 6.1.3EG (7)?

Q16: Do you agree that control of business should be demonstrated at admission and on continuous basis rather than for the entire period covered by the historical financial information? If not, then please outline your thoughts on the way in which control of business should be demonstrated.

Yes we agree with these proposals.

Independence of directors

The Corporate Governance Code

Q17: Do you agree with Option 1 or Option 2 above?

We agree with option 1.

Whilst the NAPF is a strong supporter of the flexible approach provided by the comply-or-explain mechanism of the Corporate Governance Code, we believe that where a controlling shareholder is present the principal of a majority independent board is even more vital for good governance and protection of the interests and rights of minority shareholders.

Defining independence

Q18: Do you agree with our proposed definitions of independent director and independent chairman?

We believe that the factors provided by the Corporate Governance Code remain relevant for consideration of a directors' independence.

However, given the importance of the proposal within this consultation paper to require companies with a controlling shareholder to have a board comprising a majority of independent directors, there may be scope in considering alternative ways of verifying directors' independence and the integrity of the nominations process. We believe there is merit in further exploring mechanisms to increase shareholder participation in the nomination process, especially in relation to companies with a controlling shareholder.

Application on a continuing basis

Q19: Do you support our proposal to extend the requirement for board composition as set out in LR 6.1.4ER (2) as a continuing obligation (LR 9.2.2AR(1))?

Yes, such a requirement is equally, if not more important after listing as at entry.

Period of time to rectify non compliance

Q20: Do you agree with our proposal in LR 9.2.2BR to allow for a period not exceeding 6 months from the time of notification to the FSA to rectify the non-compliance with a requirements in respect of composition of the board as set out in LR 6.1.4ER(2)?

It is unclear from the CP what the expected sanctions would be for failing to rectify non-compliance within 6 months. We believe that these principals are of sufficient importance that if a company was to flagrantly flaunt the requirements then an appropriate sanction would be to transfer the company from Premium to Standard listing.

There is a concern that 6 months will not in all cases allow sufficient time to rectify non-compliance. What is needed is a statement of intent from the company including a timeframe which should not exceed 12 months.

Election of independent directors

Q21: Do you support our proposal for election of independent directors by two rounds of voting as described above (LR 6.1.4ER (3), LR 9.2.2ER and LR 9.2.2FR)?

We believe the principal behind the proposed dual voting structure is a sensible idea and coupled with the 90 day window allows the independent investors to engage in discussion and seek an appropriate resolution. However, we do have concerns with the way the proposal is currently structured.

The 90-day cooling off period has the potential to result in a standoff between the controlling shareholder and the minority shareholders which would likely be detrimental to the company and its reputation. The "unblocking mechanism" as currently structured would only result in a satisfactory resolution if the controlling shareholder was willing to compromise or engage. Given that this proposal is being designed to protect minority shareholders from a controlling shareholder who has little concern for minority shareholder views this may be an optimistic vision.

Instead, we believe that in a situation where a controlling shareholder has in excess of 50% voting rights, then the election of independent directors should be exclusively by independent shareholders. In addition, as suggested above, we believe that especially in instances where there is a controlling shareholder there is merit in further exploring mechanisms for enhancing investor participation in the nominations process.

Mineral companies

Q22: Do you support our proposal to amend LR 6.1.9R to subject mineral companies to the requirement to demonstrate the ability to carry on an independent business together with additional requirements where a controlling shareholder is present? If you do not support this proposal, please outline your reasons for doing so.

Q23: Do you support our proposal to subject a mineral company to a continuing obligation to comply with LR 6.1.4CR, and if applicable, LR 6.1.4ER and LR 6.1.4FR at all times (LR 9.2.2AR(2))?

Yes the approach being proposed with regards to mineral companies makes sense. It is right given the nature of these businesses that the requirement to control the majority of the business should not apply, however, we agree that the independence requirements and the new proposed rules on controlling shareholders should apply to all listed companies, including mineral companies – it is often for these companies that these new requirements will be most needed.

Scientific research based companies

Q24: Do you support our proposal to amend LR 6.1.12R to subject scientific research based companies to the control of business requirement, the requirement to demonstrate the ability to carry on an independent business together with additional requirements where a controlling shareholder is present as discussed above?

Q25: Do you support our proposal to extent the continuing obligation in LR 9.2.2AR (1) to scientific research based companies in the same way as it currently applies to commercial companies? If you do not support these two proposals, please outline your reasons for doing so.

Yes we agree.

Shares in public hands (or 'free float')

Shares subject to a lock up period

Q26: Do you support our proposal to exclude shares subject to a lock up period from the calculation of shares in public hands (LR 6.1.19(4) (f))? Do you think that 30 calendar days is the right time period to dictate exclusion? Do you think that there are any other instances where shares should be excluded from a free-float calculation and if so what are they?

Yes we support this proposal.

Ability to modify the free-float requirement in the premium segment

Q27: Do you support our proposal to amend LR 6.1.20G to set out criteria based on which the FSA may modify the requirement for a 25% free float as described above?

No. While the increased transparency is of course positive, we do not support the ability to reduce the free float requirement, even in exceptional circumstances, below 25%. In our view, 25% is the bare minimum expectation to enable protection for independent shareholders invested in Premium listed companies – this corresponds with for example a Special Resolution which requires a 75% majority. We continue to believe that a 50% free float requirement should remain under consideration given that voting rights provide the foundation for ultimate minority shareholder protection.

Given the other proposals in this CP to make more use of Standard listing, we believe that the approach taken to the free float requirement for the Premium listing should be made more robust. We support more use being made of alternatives such as Standard listing for those companies who wish to float less than 25% of their shares on the public market.

Ability to modify the free-float requirement in the standard segment

Q28: Do you support our approach to companies wishing to list on the standard segment as described above?

Q29: Do you agree with the proposed criteria for assessing potential liquidity? Are there any other criteria to which we should have regard in considering the potential liquidity of shares within the standard segment?

We are open to the idea of greater flexibility being provided for entry to the standard segment. We believe this proposal further emphasises the case for a more robust approach to be taken on this issue in relation to companies seeking a Premium listing.

The development and promotion of the Standard segment should be a priority to ensure that there is a natural and appealing home for less mature fast-growing companies wishing to list in London whilst protecting the reputation and integrity of the Premium segment.

Holdings of individual fund managers

Q30: Do you agree with the proposed new guidance in the Listing Rules (LR 6.1.20AG) clarifying that holdings of individual fund managers in an organisation will be treated separately provided investment decisions with regard to the acquisition of shares are made independently?

Financial instruments with a long economic exposure to shares

Q31: Do you agree with the proposed new guidance in the Listing Rules (LR 6.1.20BG) explaining that we consider that financial instruments that give a long exposure to shares, but do not control the buy/sell decision in respect of the shares, should not normally count as an interest for the purpose of the public hands threshold?

We agree.

Continuing obligations

Voting by premium listed shares

Q32: Do you support our proposal in LR 6.1.25R and LR 9.2.22R to require that where a shareholder vote must be taken under the provisions of LR 5.2, LR 5.4A, LR 9.2.2CR, LR 9.4, LR 9.5, LR 10, LR 11, LR 12 or LR 15, such votes must be decided by a resolution of the holders of premium listed shares as discussed above?

We agree.

Guidance on LR 9.2.22R

Q33: Do you support the FSA having the power to modify the requirement imposed in LR 9.2.22R in exceptional circumstances (LR 9.2.23G)? Are there any other exceptions that should be specifically catered for within this guidance?

Yes this is appropriate for the types of exceptional circumstances outlined.

Duty to notify the FSA of non-compliance

Q34: Do you support our proposal to delete LR 9.2.16R and replace it with a requirement in LR 9.2.24R for a listed company to notify any non-compliance with continuing obligations as set out in LR 9.2 to the FSA without delay?

Yes, this is important for the reputation and integrity of the Premium segment.

Cancellation or transfer of listing category

Q35: Do you support our proposal to delete LR 9.2.17G and replace it with guidance in LR 9.2.25G to consider LR 5.2.2G (2) and LR 5.4A.16G in relation to its compliance with the continuing obligations as set out in LR 9.2?

We agree that where a listed company is not complying with its obligations it should transfer to a Standard listing. As stated before, it is vital for the reputation and integrity of the Premium listing that an expectation of adherence to high levels of corporate governance are maintained. We would welcome further clarification about how this would be enforced.

Disclosure in the annual report

Q36: Do you support our proposal to amend LR 9.8.4R to require a listed company to disclose all matters that need to be disclosed under LR 9.8.4R in the annual report and accounts in a single identifiable section?

Yes, the annual report disclosures are a vital and it is important that they are clear and identifiable. Many annual reports are too long and cluttered and therefore this proposal supports efforts being made elsewhere to improve reporting and make annual reports more accessible and understandable for shareholders.

Disclosure of smaller related party transactions in annual report

Q37: Do you support our proposal to amend LR 9.8.4R(3) to extend the period of time over which disclosure of smaller related party transactions as required by LR 11.1.10R(2)(c) should be included in the annual report and accounts to include comparative information for the previous 2 financial years?

Q38: Do you support our proposal to amend LR 11.1.10R(2)(c) to set out minimum disclosure requirements that need to be set out in the listed company's next published annual accounts as described above? Do you think that there are other factors relating to the smaller related party transaction that should be subject to disclosure requirements in the company's next published annual accounts and if so what are they?

Yes this is a welcome proposal and will greatly assist shareholders ability to monitor these important disclosures and identify any concerning trends.

Warrants or options to subscribe

Q39: Do you believe that we should introduce a continuing obligation that a listed company must comply with LR 6.1.22R at all times (LR 9.2.21R) or alternatively that we should delete the existing eligibility requirement?

Yes we would welcome the introduction of a continuous obligation to comply with LR 6.1.22R.

The Listing Principles

Application

Q40: Do you agree with our proposal to amend LR 7.1.1R to make Listing Principles applicable to standard listed issuers?

Yes, we agree that certain principles apply to all listed companies and therefore welcome this change, however, we do not understand why the FSA considers Principles, 1, 3 and 4 are not relevant for all listed companies.

Principle 6 – open and co-operative

Q41: Do you support our proposal to amend LR 7.2.1R as described above? If not please provide an explanation for objection to each principle.

Yes we believe it is appropriate that all listed companies adhere to the two suggested principles: 1. take reasonable steps to establish and maintain adequate procedures, systems and controls, and, 2. deal with the *FSA* in an open and cooperative manner. As above however, we do not understand why the FSA considers Principles, 1, 3 and 4 are not also relevant for all listed companies.

Guidance on the Listing Principles

Q42: Do you support our proposal to amend the guidance in LR 7.2.2G and 7.2.3G to enable the application of the guidance to the relevant Principles?

Yes.

Continuing obligation arising from Premium Listing Principle 1

Q43: Do you support our proposal to amend LR 9.8.6R (5) by including a specific disclosure obligation on the application of Principle B4 of the Code along with the accompanying guidance in LR 9.8.6BG?

Yes we believe that this a positive change and will provide shareholders with additional information with which to judge whether a company is doing enough to ensure that the directors are up to date with the applicable regulations.

Premium Listing Principle 3 – voting power of a premium listed share

Q44: Do you support the requirement that each premium listed share in a class must have equal voting power (Premium Listing Principle 3)? If you do not support this principle, please outline your view on how the listing regime can operate effectively if shares within the same class have various voting power.

Yes, the NAPF believes that each premium listed share in a class must have equal voting weight. In addition, we believe that in relation to conventional companies, consideration should be given to only allowing issuers in the Premium segment to issue a single share class.

Principle 4 – aggregate voting rights of the shares in each class

Q45: Do you support the requirement that, where a company has more than one class of equity shares admitted to premium listing, the aggregate voting rights of the shares in each class should be broadly proportionate to the relative interests of those classes in the equity of the company Premium Listing Principle 4)?

Yes, however, we do believe that in relation to conventional companies, consideration should be given to only allowing issuers in the Premium segment to issue a single share class.

Guidance on Premium Listing Principle 4

Q46: Do you support our proposal for guidance on Principle 4 (LR 7.2.4G) as to the factors the FSA will have regard to in assessing whether the voting rights are proportionate? Are there any other factors that the FSA should have regard to in applying this principle and if so what are they?

Implementation of AIFMD

Q47: Do you agree with our proposed approach to articulate in the Listing Rules our expectations of the board of a premium listed investment entity rather than use a more prescriptive solution?

Q48: Do the proposed rules capture adequately the role of the Board?

We support these proposals.