Disclosure, Financial Misconduct and Listed Companies: A Critical Analysis of the UKLA's Continuing Obligations Regime

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INTRODUCTION

This paper is aimed predominantly at the critical examination of the continuing obligations regime imposed on listed public companies via the United Kingdom Listing Authority's (UKLA) Listing Rules. It will examine to what extent the continuing obligations provide adequate protection for a company's shareholders (as well as potential investors, ie the general public) against, *inter alia*, financial misconduct by the directors of their companies. The importance of shielding shareholders, and others, from such misconduct, has been exacerbated by recent corporate scandals in the USA that have had far-reaching effects on their heavily dispersed membership base.

A steady stream of financial scandals has rocked the world of business in recent times. As a result, the regulation of financial information — and, more importantly, the detection and prosecution of gross misconduct and fraud on the part of directors of large corporations — has become the focus of considerable discourse, both in the news media and in the legal academic world. The issue of prosecution (by both the mass media and the courts) has more recently been concentrated in the USA; however, the sheer size and global nature of the corporations involved mean that the issues are nevertheless of international significance. In any event, the United Kingdom is not exactly impervious to such scandals; the names Maxwell and Hollinger spring to mind. Disclosure of information to the shareholders and to the public has therefore become an unavoidable requirement.

Because of those various financial scandals that have rocked the corporate world in recent years,[1] aided by the increasingly proliferated news media, numerous proposals have been put forward to counter what is essentially accounting fraud.[2] The condition, somewhat cheekily dubbed 'Enronitis' by one commentator,[3] involves 'rapidly advanced and ill-thought-out courses of action which shift the responsibility for doing anything onto someone else'.[4] Apart from these scandals, the importance of reliable (and accurate) accounting information is self-evident. This is so, as 'accounting information has economic consequences, since such information influences decisions concerning the allocation of scarce economic resources'.[5] As a result, the UK Accounting Standards Board decided to review the UK Accounting Standards to counter the possibility of an Enron-type scandal occurring in the UK.

The need for continuing obligations arises almost innately out of the need for the law to protect modern shareholders against possible malpractice by their company's directors. This is important because of the increasing tendency toward shareholding in large corporations as a short-term investment mechanism. Such short-termism means that shareholders are detached from the day-to-day running of their company and so have little control over the movement of the business or of the manner in which their investment is being utilised. The fact that such interim investments are in vogue necessitates that such vulnerable members of a listed public company are adequately insulated.

The Continuing Obligations Guide,[6] produced by the Financial Services Authority (FSA) in its capacity as the UKLA and designed to serve as a synopsis of the continuing obligation regime, outlines in paragraph 1.4 two underlying principles behind all continuing obligations promulgated in the listing rules:

- timely disclosure of all relevant information; and
- equal treatment of all shareholders.

The aim of the former is to effect mandatory disclosure of all relevant information about a listed company's business on a continuing basis, to ensure that the market and the general public are not kept in the dark as to information which may impact on their various decision-making thought processes. The latter principle is self-explanatory, as it mainly serves to ensure that all the members of a company are treated in an identical manner: that is, requirements such as the timely disclosure of information must be fulfilled in respect of all the shareholders of the

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company. The increasing proliferation and diversity of shareholders in contemporary companies means that shareholders have little or no control, or even input, in the day-to-day running of their company's affairs. This fact makes the need for equality in the treatment of such a diverse range of shareholders of paramount importance under the continuing obligations regime.

Whilst corporate governance *per se* is not the precise subject matter of this research, it should be borne in mind that it is, nevertheless, the fundamental basis for continuing obligations; as such, it is expected to be a recurring concept in this paper. In essence, continuing obligations may be best viewed as representing a small aspect of the much wider scope of corporate governance.

Continuing obligations are 'continuing' by their very nature: they continue to apply to public companies even after the initial set of requirements have been complied with in the process of listing or quotation, and in any case, a listed plc must continually have regard to them. These continuing obligations are a combination of the requirements of the single financial regulator, the FSA; UK legislation; and European Union Directives.[7]

The obligations to be considered are:

- Disclosure of information (Listing Rules (LR), chapter 9)
- Transactions, including related-party transactions (LR chs 10, 11)
- Financial information (LR ch 12; Companies Act (CA) 1985, Part VII and schedules 4–11)
- Communications with shareholders (LR ch 14; LR 9.24)
- Directors (LR ch 16 and the Model Code)
- Buy-back of shares (LR 14.16 and ch 15; CA 1985, ss 143–170 and 277).

These obligations are, presumably, not exhaustive; additional obligations, perhaps in response to the perpetually changing markets, will be added as deemed fit by the UKLA. The effectiveness of these obligations in fulfilling their purpose of investor/public protection is the essence of this research. Whilst they are not purported to be the only mechanisms conferring continuing obligations on listed public companies, it is proposed that they are the most significant ones in effecting a practical approach to investor/public protection.[8] In the following sections each of the obligations will be examined critically.

DISCLOSURE OF INFORMATION

Introduction

The flow of information from a listed public company to the general public via the market is a major aspect of its continuing obligations. It is aimed at the distribution of information that might be expected to affect the company's share price. Any incident which, if made public, may influence the share price of a company inevitably leads to trading in the company's listed securities. For example, news of a proposed takeover bid is certain to affect almost instantaneously the price and value of listed shares. The obligation to disclose such information can, broadly speaking, be categorised into general and specific disclosure requirements.

The general obligation

Such information is disseminated via any one of the five *Primary Information Providers*. LR paragraph 9.1(a) provides that a company must notify a regulatory information service (RIS) without delay of any major new developments in its 'sphere of activity'. This refers to developments which are not yet in the public domain and which may lead to substantial movement in the price of its listed securities. 'Sphere of activity' denotes a wide duty of disclosure, since it seems to catch even information that does not directly relate to the company. The idea is that the general public is given access to information that is unique to the field or sector in question. In essence, information which may otherwise be considered as inside or specialist information but which may affect share price must be revealed. David Keeling[9] believes that, as a result, a company would have to disclose information regarding, say, a technological breakthrough made by a competitor that would result in the company's major product becoming outmoded.[10] Arguably, this appears a rather extreme requirement, as a company would be forced to assess the likelihood of a competitor's product superseding its own. On the other hand, where a company's wealth, and perhaps market dominance, is dependent on a single product, the introduction of a superior product by a competitor is bound to reduce the company's ability to compete in that marketplace and thus diminish its viability as a good investment apparatus.

Paragraph 9.2 of LR goes further, to require the disclosure of information concerning a change in the company's financial position, the performance of its business, or even the company's expectations as to its performance that is likely to lead to substantial movement in the price of its listed shares. The aim of investor protection is achieved here through the provision that the company effects the compulsory availability of price-sensitive information. This in turn provides the otherwise unsuspecting potential investor with adequate information on which to make an informed decision. In relation to such unpublished price-sensitive information, the FSA's Guidance Note provides that whilst companies are encouraged to assist analysts where possible in forming a view of their activities and trading prospects, they should, nevertheless, decline to answer analysts' questions where answering would provide price-sensitive information.

One must be aware of the importance of balancing both investor and public protection. The goal of public protection is set so highly that paragraph 9.7 of the LR provides that even information proposed to be announced at a company's general meeting (with the potential of significantly affecting share price) must also be announced to an RIS, so as to ensure that such announcements are simultaneous. This is to ensure that not even a company's shareholders can be afforded superior protection in terms of the body corporate's continuing obligation of disclosure. A further incentive for a company to abide by this obligation is that, aside from being in breach of its continuing obligations, failure to disclose may also constitute an offence under section 397 of the FSMA.[11] Against the risk that this appears too stringent and disproportionate, paragraphs 9.4 and 9.5, as a balancing factor, provide exceptions for information about impending developments or matters in the course of negotiation. In addition, the UKLA may make an exemption for a company where disclosure of information to an RIS might prejudice its legitimate interest.[12]

Specific disclosure

In addition to such general disclosure obligations, the UKLA LR provide for the disclosure of specific items of information to an RIS. These are in respect of information relating to capital; to major interests in shares; to instances when an RIS is not open for business; and to rights as between holders of securities.

In relation to capital, paragraph 9.10 compels a company to notify an RIS of information relating to such matters as alterations to capital structure; new issue of debt securities; redemption or drawing; and issues affecting conversion rights and the like. This will ensure that the company is not able to alter the capital structure of its business without having to disclose it publicly. An incentive is inherent therefore that a company wishing to engage in any of the specified matters must consider the impact or impression it might create in the wider market.

In relation to major interests in shares, paragraph 9.11 provides that a company must disclose to an RIS any information disclosed to it in accordance with sections 198 to 208 of the Companies Act 1985.[13] Paragraph 9.12 requires the disclosure of any information obtained by it pursuant to section 212 of that Act.[14]

In the event that the Listing Rules require notification to an RIS at a time when it is not open for business, the company must ensure that it discloses such information instead to at least two national newspapers and two newswire services in the UK. The information must still, of course, be disseminated to an RIS as soon as it opens.

In respect of rights as between holders of securities, paragraphs 9.16 and 9.17 provide for equal treatment of all holders of securities in the same position. Also, note that the section 89[15] pre-emption right is replicated in paragraph 9.18, with a relaxation in paragraph 9.19.

In addition to notification as per capital as already discussed above, the aim of investor protection is accomplished effectively through paragraph 9.22, which obliges companies to obtain the consent of their shareholders before any major subsidiary undertaking of the company[16] makes any issue for cash of equity securities which will result in material dilution of the company's percentage interest in the shares of that subsidiary. Other notifiable information includes board decisions on dividends, profits and other matters requiring announcement;[17] the fact that the proportion of listed equity shares of any class in public hands has fallen below 25 per cent;[18] and change of name.[19]

There are other specific disclosure requirements elsewhere in the LR. For instance, paragraph 15.3 provides that any decision by the board to submit to shareholders a proposal for the company to be authorised to purchase its own securities (other than the renewal of an existing authority) must be notified to an RIS.[20]

It is perhaps helpful, for the sake of completeness, to note that the misuse of price-sensitive information may result in civil claims being instituted against a company. This is so, as Henderson opined, since compliance with FSMA requirements does not necessarily extinguish the risk of successful claims being initiated in the civil courts.[21]

Conclusion

The depth of disclosure required of listed public companies should provide a wealth of information for investors and potential investors alike. As the world of financial services is a volatile one in which time is of the essence, the speedy time requirements of appropriate disclosures are proper. The recurring nature of the disclosure of financial information is an important aspect, as it ensures that companies continue to update their shareholders and the market on changes in their financial position, business performance, expectations and other matters which are likely to lead to substantial movement in the price of their listed shares. Others include alterations to capital structure and the new issue of debt securities. The importance of maintaining a balance between investor and public protection is also emphasised: for example, the information proposed to be announced at a company's AGM (which may affect its share price) must also be announced to an RIS.

TRANSACTIONS

Introduction

Notwithstanding the fact that the members of a company cede control over their investment to the board of directors, there remains the necessity to protect those shareholders in major situations. That is, the fact that professionals are given the power to direct and control a business does not preclude its owners from being able to exercise some degree of constraint, especially when the company intends to enter into major transactions which may have a profound effect on the company's standing, or where transactions are with related parties.

The rules governing transactions entered into by a listed public company are designed to ensure that shareholders are kept informed of such transactions. More importantly, perhaps, they are also designed to have the effect of subjecting certain transactions — of a large nature — to shareholder democracy. The rationale for the latter is, of course, to give the shareholders an opportunity to accept or reject major transactions that may significantly affect their company, in terms of its strategic direction, business focus or even gearing ratio.

Class tests[22]

Chapter 10 of the LR commences by outlining the transactions covered. The latter are: transactions by any subsidiary of the listed company; and the grant or acquisition of an option (which will be classified on exercise and only the consideration for the grant will be classified).[23] The obligation on a listed company in this regard depends on the classification of transactions, as those requirements differ depending on the class they fall into. This in turn depends on the size of the transaction being entered into. The listing rules set out various *size tests* for such classification.[24] Transactions are grouped by comparing the size of the transaction with that of the listed company engaging in it.[25]

As indicated by paragraph 10.17 of the listing rules, the figures used for classification purposes must be those shown in the company's latest published audited consolidated accounts. Alternatively, where a company has, or will have, published a preliminary statement of later annual results at the time of agreeing the terms of the transaction, those preliminary figures should be used instead. In respect of the market capitalisation test,[26] the requisite figure is the aggregate market value of all the ordinary shares (excluding treasury shares) at the close of business on the last day immediately preceding the announcement. In the event that a company has published a balance sheet as part of its half-yearly report, paragraph 10.19 states that that balance sheet must be used for the purpose of classification. The essence here is that the figures used do not become outdated and so present only a distorted view of the size of a given company or of the class of a given transaction. Classification must therefore seek to utilise the latest available figures, since during the course of negotiation significant changes may have occurred that may have somewhat altered the percentage ratio of a transaction and thus the regulatory requirements of the UKLA under the listing rules.[27]

Reverse takeovers

There are certain exceptions to the classification rules in the case of a reverse takeover, in which case such a transaction will be automatically treated as a class 1[28] transaction provided certain conditions are satisfied. Those exceptions, as laid out in paragraph 10.21, include where:

- the target company is of a similar size to that of the acquiring company;

- the target company is in a similar line of business to that of the acquiring company;
- the undertaking of the target complies with the *conditions for listing* set out in chapter 3; or
- there will be no change of board or voting control.

If any of these is the case and the transaction is classified as a reverse takeover, it is a class 1 transaction and so subject to the most extensive and stringent of the continuing obligations imposed in the context of transactions.

An obvious way to attempt to avoid compliance is to carry out related transactions in smaller segments, so as to avoid subjection to class 1 requirements. However, as paragraph 10.25 provides, the UKLA 'may require transactions completed during the 12 months prior to the date of the latest transaction to be aggregated with the latest transaction for the purpose of determining the classification to apply to the latest transactions'. As always with regard to the listing rules, for the avoidance of doubt the UKLA should be consulted early for advice and, where appropriate, directions should be sought from the UKLA. The safest option for a listed company in the course of a transaction which amounts to a reverse takeover under paragraph 10.4(d) is to comply with the requirements for class 1 transactions.[29]

In conclusion, the need for the classification of transactions stems from the desire to afford proportional protection to shareholders of listed companies depending on the size of the transaction and thus its likely impact on the company. The need for the latter itself stems from the desire to give additional protection to the public and to the shareholders, who are nowadays generally vast in numbers because of the ease of trading in shares (liquidity) and the attractiveness of short-term profit-oriented shareholding.

Related-party transactions (RPT)

The rationale for the regulation of transactions with related parties is self-evident, since it seeks to limit the scope within which a person closely connected with a company may do business with the company in secret. This is especially important where a company director seeks to enter into transactions with his own company and is therefore on both sides of the agreement. Transactions with related parties, like reverse takeovers, have annexed to them continuing obligations requirements tantamount to those of class 1 transactions. In this case, it is not the size of the transaction but the relationship between the contracting parties that determines its classification. A related-party transaction (RPT), as governed by chapter 11 of the listing rules, is defined as:[30]

'(i) a transaction (other than a transaction of a revenue nature in the ordinary course of business) between a company, or any of its subsidiary undertakings, and a related party;
(ii) any arrangements pursuant to which a company, or any of its subsidiary undertakings, and a related party each invests in, or provides finance to, another undertaking or asset; or
(iii) a transaction (other than a transaction of a revenue nature in the ordinary course of business) between a company, or any of its subsidiary undertakings, and any person who, or other entity which exercises significant influence over the company. . . '

In essence, any transaction involving a listed public company and a related party or any person exercising a significant influence over the company is covered under this chapter. Such transactions are not prohibited; instead they are closely regulated. The rationale is, of course, to protect shareholders from possible improprieties by their directors, especially when those directors have an interest, direct or otherwise, in a company transaction. The listing rules provide safeguards to insulate the company's owners against such actions by the chosen few who actually run it on their behalf.

There are three principal categories of related party defined in the listing rules, namely:[31]

- a substantial shareholder of the company;
- any director or shadow director of the company (or its parent or subsidiary) or a fellow subsidiary undertaking;[32] and
- an associate of a person falling under either of the two above categories.[33]

In the event that a person is adjudged a related party in the context of a company transaction, paragraph 11.4 dictates that the company must make an announcement to an RIS, send a circular to its shareholders, obtain the approval of shareholders and, where applicable, ensure that the related party and his associates abstain from voting on the relevant resolution.[34] It is needless to say that the announcement must comply with the requirements of LR chapter

10 and must contain the name of the related party and also the details of the nature and extent of his interest.

Certain transactions, notwithstanding their related-party aspect, are exempted from the disclosure and shareholder democracy requirements of chapter 11.[35] Those exemptions apply to situations ranging from where the company does not have equity securities listed, is an overseas company,[36] or is selling treasury shares, to the grant of employees' share schemes and small transactions.[37]

Conclusion

The culture of short-termism when investing in companies and the associated vastness of membership base necessarily result in those shareholders having less control over the daily management and strategy of their company. It is, therefore, imperative that they are made aware of certain major transactions involving their company and also allowed to exercise a decisive influence over even larger transactions. It is arguable, of course, that those shareholders would not want to, or are not able to, participate in the daily running of their companies anyway, but even the admitted credibility of this supposition fails to detract from the pressing need to subject certain major transactions to shareholder democracy.[38]

The reasoning behind the regulation of related-party transactions is evident, as it serves to publicise shadowy transactions which sometimes occur between a company and those connected to it. These transactions are not in themselves undesirable, since they may well be in the company's good interests; however, the close proximity between the company and related parties means that the boundaries of contractual and fiduciary duties and responsibilities may become obscure. In any event, it may well be that a director is a decision maker for both the company and a contracting party vis-à-vis a company transaction, in which case conflicts of interests are liable to arise.

FINANCIAL INFORMATION

Introduction

Many of the corporate scandals that have besieged the world of business and dented public confidence in large multinationals were made possible by a fraudulent use of financial information, of which accounting data are paramount. Therefore, in achieving the ultimate goal of investor protection, the production of credible financial information by the company to its members is of indubitable importance. It is contended that a company's relative health, or otherwise, can, after all, often be judged on the basis of its accounting information. Therefore, the accuracy of such information is deemed vital, as it tends to serve as an influential factor in an investor's reckoning as regards his remaining a member of a company or not. The convoluted nature of accounting information means that there is scope for a company's directors to manipulate, to a great degree, the outlook of the company, through a propagandist use of figures. One would recall that misstatements in financial information enabled such far-reaching corporate scandals as Enron, WorldCom, Adelphia and Tyco to happen.

In light of this, the relevance of auditors and, more importantly, the competent regulation of auditors have become increasingly indispensable. This is so since, in order to safeguard the rights of shareholders to receipt of accurate financial information, there has to be a mechanism through which the information provided by companies can be both analysed and verified. The directors of a company need to be put in an agency position in relation to the shareholders, so that they realise that their actions must not only conform to the wishes of shareholders but also be in the best interests of their principal, the shareholders. It is for this reason that Bagheri stated that '[c]orporate governance mechanism and at its heart the auditing and rating systems have evolved to mitigate agency problems of this nature'.[39] It is also for this reason, following the Enron scandal, that the UK government announced two separate reviews into the country's arrangements for financial reporting and auditing.[40] The British response to Enron has been swift, as the Auditing Practices Board is also said to be assessing the implications of the debacle for UK auditing standards.[41] In addition, the UKLA and the Accounting Standards Board have both commenced reviews aimed at limiting the possibility of such financial catastrophes occurring in the UK.[42]

A great deal of regulation is, therefore, applicable to listed company's obligation to disclose financial information. Such obligation is largely in respect of the disclosure of accounting information (annual accounts and interim reports) and profit forecasts, as regulated by the listing rules and the Companies Act 1985.

Annual and interim report and accounts

As a starting point, section 221 of the Companies Act 1985 imposes the obligation that every company keep accounting records in accordance with the provisions of the Act. Further, subsection (5) renders failure to comply with section 221 a criminal offence punishable, under subsection (6), by imprisonment or fine or both. The directors of a group of companies, in addition to preparing individual accounts, must also prepare consolidated accounts.[43] A firm of independent auditors must, of course, be contracted to audit the accounts.[44]

LR paragraph 12.41 requires that a listed public company must issue an annual report and accounts. Paragraph 12.42 adds substance to this requirement: for example, paragraph 12.42(b) requires that the annual report and accounts be independently audited in accordance with auditing standards required in the UK or the USA or by International Standards on Auditing. A listed company must publish its audited annual report and accounts not later than six months from the end of the financial period to which they relate.[45] The depth in the level of regulation of listed companies by the UKLA, as contained in the listing rules, is evident in paragraph 12.43, which outlines, with a considerable degree of precision, the items that must be included in the annual report and accounts.[46]

A listed company's continuing obligations go further, to require that listed companies also publish an interim report (including profit and loss accounts) for the first six months of the financial year. The publication deadline for this is 90 days from the end of the period to which it relates. While it need not be audited, it must be stated clearly if it has not been. In respect of the half-yearly report, needless to say, the listing rules, via paragraph 12.47, require that the accounting policies and presentation employed for the interim figures be consistent with those applied in the annual accounts, the logical exception being where such policies are to be changed in subsequent annual financial statements. Further, the information that must be contained in the interim report is dictated in LR paragraphs 12.52–12.56. Flexibility, if required, is catered for in paragraph 12.57: the UKLA may require suitable adaptations to be made when certain requirements of the listing rules are deemed unsuited to a given company's particular circumstances. In any event, paragraphs 12.58 and 12.59 provide that the UKLA may authorise the omission of certain pieces of information from a company's interim reports in appropriate instances.

The increasing layer of obligations imposed on listed public companies, as compared with public companies generally, is evident in respect of the financial information required to be provided by the board of directors. In addition to accounting information, LR paragraph 12.43A instructs that a listed company must include in its annual report and accounts a narrative statement of how it has applied the principles set out in section 1 of the Combined Code.[47] The latter deals with, *inter alia*, information as to directors' remuneration ranging from its level and make-up to the disclosure of the remuneration policy and, in fact, details of the remuneration of each director. In plain words, every director's salary must be stated.

That level of disclosure would seem absurd in the context of a private company and perhaps even for small public companies. However, it is submitted that the nature of the contemporary listed public company renders it necessary that such disclosure is effected.[48] The distance between the company's numerous members and those few who run it means that in order to afford any worthwhile degree of protection to the members, such extensive disclosure requirements, and perhaps more, are needed. In essence, the diverse nature of shareholders in modern listed companies necessitates that stringent controls be put in place for the protection of those who, after all, have provided the capital with which the company's business is run.

Paragraph 12.45 provides that where a listed company issues a summary financial statement, it must disclose earnings per share in addition to the required contents for summary financial statements contained in the Companies (Summary Financial Statement) Regulations.[49] This is clearly so that those receiving only the summary financial statements are not unduly disadvantaged.

Profit forecasts

The regulation of financial information under the listing rules extends also to profit forecasts published by a listed body corporate.[50] Corporate profit refers to an 'increase in the ownership interest in a company';[51] that is, an increase in the value of the members' equity shares in it. A profit forecast is simply an estimate of such an increase for the last unaudited accounting period, the current accounting period or a future accounting period.[52]

Ogowewo articulates the need for the regulation of profit forecasts with considerable precision.[53] He proposes three main reasons why forecasts published by companies should be regulated.[54] Firstly, a defensive profit forecast could amount to a frustrating action in the context of a proposed takeover. He argues that, whilst a defensive profit forecast does not ordinarily amount to a frustrating action, 'a misleading profit forecast is likely to corrupt the decision-making process of target shareholders'.[55] Secondly, if left unregulated, profit forecasts may be inaccurate or misleading. This is an important point in that the provision of relevant but also accurate information is at the forefront of the continuing obligations regime. Thirdly, there is the need to prevent market manipulation. Such manipulation can occur where a misleading profit forecast is made by a bidder in a share-for-share offer in an attempt to make its securities appear more attractive; or by a defensive target board to discourage its shareholders from accepting a bidder's offer. Market manipulation is seen as a market evil that has to be battled rigorously and, therefore, various regulatory bodies play a part in its prevention and detection. Note that the FSA also plays an important part in this, in carrying out its role as the single financial services regulator.

LR paragraph 12.23 provides that a calculation of an approximate figure for future profits or losses is a profit forecast, even in the absence of a specified figure and/or the word 'profit'. Paragraph 12.24 further requires that a company's profit forecast must be reported on by its auditors or reporting accountants and by the sponsor in certain circumstances.[56] It adds that the accountants must state whether, in their opinion, the forecast has been properly compiled on the basis stated and that the basis of calculation is consistent with the accounting policies of the company. See also paragraphs 12.27 (in respect of assumptions)[57] and 12.43(b) (commentary on forecasts).[58]

Conclusion

In conclusion, it is clear that an extensive amount of information is required of a listed public company in respect of the financial state of the company. Such detailed disclosures can then be analysed by the financial advisers of the company's investors, as well as by potential investors. The result is that they are able to make more suitable investment decisions. In any event, the decision as to whether or not to deal in one's shares in a company or whether or not to invest in a company can be an informed one. The prudence of investing in any given company is of course a concern for the investor and not the UKLA. The latter is concerned only that adequate disclosures have been made to enable an informed decision to be made.

COMMUNICATIONS WITH SHAREHOLDERS

Introduction

There are various mechanisms available to a company's directors for communicating with shareholders. These range from notices in the national press to circulars sent out to each shareholder. Communication is required in a variety of circumstances. For example, where shareholders are notified of a meeting to deal with issues other than ordinary business at the company's annual general meeting (AGM), the notice must incorporate an explanatory circular.[59]

One of the underlying principles of the continuing obligations regime is the equal treatment of all shareholders. One way for a company to show that it has complied with this is to disclose identical information to all shareholders and at the same time. An effective means of doing this is by sending out information in the form of a circular. In any case, the listing rules require compulsory sending of circulars to shareholders in certain circumstances: for example, in respect of a class 1 transaction.

The UKLA's guide to the continuing obligations regime defines a circular as:[60]

> 'any document issued to holders of listed securities including notices of meetings but excluding listing particulars, annual reports and accounts, interim reports, proxy cards and dividend or interest vouchers.'[61]

Information is often disclosed to shareholders through circulars as stated above. It is needless to say that the aim of investor protection is also at its forefront. One of the most important ways of protecting investors is through the regulation of the company's communications with its shareholders. Requirements regarding circulars fall into two main categories: general[62] and specific.[63]

General requirements

LR 14.1 provides that a circular sent by a company to holders of its listed securities must include, *inter alia*, a clear and adequate explanation of its subject matter; all necessary information; and, where voting is required, a recommendation from the directors as to the voting action that shareholders should take. The requirement of clear and adequate explanation of a circular's subject matter is an objective test. That is, the board of directors is expected to provide such information as a reasonably competent board would deem appropriately relevant (and adequate) in presenting a clear and accurate picture to the shareholders. In relation to voting, paragraph 14.1(b) requires that a circular contain *all necessary information* to enable the shareholders to make an informed decision: again an objective test, which directors should construe generously to ensure that they comply with the listing rules. Where new securities are being proposed for listing, a circular must state that an application has been or will be made for the securities to be admitted to the Official List. Paragraph 14.1(h) goes on to outline other matters that should be included in the circular, if known at the time of the communication: for example, the ranking of the new securities in terms of dividend, interest and existing listed securities. In addition, paragraph 14.1(i) provides that where a person is named in the circular as an adviser, the circular must include a statement that such adviser has given and has not withdrawn its written consent to the inclusion of its name in that particular context.

The extent of information to be provided to shareholders by directors via circulars would appear to be left to the board to decide, save for the general guidance given in paragraph 14.1. It is not inconceivable that directors might proceed to provide inadequate information, though in compliance with 14.1, thereby (legitimately) sending an ambiguous message to shareholders, as a result of the complex nature of a public company's business. As a way of mitigating this, however, paragraph 14.2 further provides that there be formal approval of circulars by the UKLA prior to their being sent out to the shareholders.[64] That is, the company must send three copies of the draft circular to the UKLA so that the contents can be verified as having complied with the regulatory standards set by the listing rules. It is worth noting that the rules could have simply provided an avenue through which shareholders could seek redress in the event of their being given false information. It is a measure of the importance of insulating investors from receiving defective information and dealing in their investments as a result that they are shielded from receiving such material in the first place. Further, following the requisite approval, the company must still lodge two copies of the circular in its final form with the UKLA, to ensure that there are no subsequent alterations.[65] Paragraph 14.5 creates an exception: that certain circulars (eg those of a routine nature) need not be lodged with the UKLA for approval prior to publication.[66] Paragraphs 14.7–14.26 serve to add substance to this exception.[67]

Specific requirements

In respect of the specific requirements, parts of chapters 9, 10, 11, 13 and 15 are relevant. Paragraph 9.24, which deals with companies with securities listed in other European Union member states, provides that a company must ensure that all the necessary facilities and information required to enable members to exercise their rights are made available in each member state where their securities are listed. Particular attention is paid to the publication of notices (or the distribution of circulars) in respect of the allocation and payment of dividends and interest; the issue of new securities; and the redemption or repayment of securities. A company must also communicate details of meetings which holders of securities are entitled to attend and, of course, provide them with facilities to implement their right to vote where applicable. The relevance of this provision is apparent in that it ensures that the treatment of UK-based holders of securities is identical to the equal treatment of those holders of the company's securities in other member states — in fulfilment of the underlying principles. However, its pragmatic importance or necessity is questionable, since each member state will invariably have its own requirements imposed on companies in respect of their shareholders in that member state.

Paragraph 10.37 states that in respect of a *class 1* transaction, the company must send an explanatory circular to its shareholders. The content of such a circular is outlined in paragraphs 10.40–10.43. Paragraph 10.40 requires the company to include in a class 1 circular all the information listed in the Appendix to chapter 10. As regards a profit forecast, following an acquisition (or a disposal) a forecast may be contained either in a single statement or in separate statements for the listed company and its subsidiary undertakings.[68]

Paragraph 11.10 provides that a circular concerning a related-party transaction must include certain other specified pieces of information in addition to the general requirements in chapter 14. LR 11.10(a) states that a circular must include certain information about the company as outlined in certain sections of chapter 6.[69]

LR 15.4 states that a circular seeking shareholders' authority for the company's purchase of its own shares must contain a number of things. These include a statement as to the directors' intentions regarding the utilisation of the authority and details regarding the price etc; any outstanding warrants and options to subscribe for equity shares; and the proportion of the company's issued share capital (with the exclusion of treasury shares) that they represent, both before and after use of the authority.[70]

Conclusion

In conclusion, it is the writer's contention that the requirement that the UKLA's prior approval be sought for circulars proposed to be sent to a company's shareholders is one of the most effective mechanisms of investor protection promulgated by the listing rules. The proliferation of shareholder base has meant that the members of a company depend on adequate information being provided to them by the company in order to inform their decision-making thought processes. Such reliance inevitably makes shareholders susceptible to board manipulation. The absence of an alternative source of credible information makes the situation even more critical. It is in this light that the listing rules compel the board to submit draft copies of most circulars to the FSA in its capacity as the UKLA for prior approval. In any event, copies of the final circular (whether required to be lodged for prior approval or not) must be lodged with the UKLA for confirmation of compliance and as a further deterrent to otherwise unscrupulous directors.

DIRECTORS

Introduction

Directors of large corporations have come under intense scrutiny following the financial scandals that have engulfed the corporate world. This is because, notwithstanding the separate legal personality of companies and the associated veil of incorporation, it is the directors who, as the human agents of a company, exercise actual control over its affairs. Therefore, where there is a fraud, it is usually perpetrated by the directors or under their instructions or with their knowledge, constructive or otherwise. The Enron debacle has led to the prosecution of many directors as well as of their financial advisers.

It should be noted here that directors' duties contained in chapter 16 of the Listing Rules, as well as in the Model Code contained in the Appendix to that chapter, are not strictly part of the continuing obligations imposed on listed public companies *per se*, since they do not directly relate to companies. The rationale for their discussion in this context is explained below.

General law — statute and common law — imposes a great deal of obligation on company directors. An examination of those duties is well outside the scope of this essay. However, the listing rules provide additional obligations applicable only to the directors of listed public companies, which are added to the existing body of duties and obligations conferred on directors generally. It is this additional set of rules, culminating in an extra layer of regulation, which forms the subject matter of this section of the research. The justification, therefore, for the treatment of directors in this paper is that the obligations to be discussed are part of the continuing obligations regime imposed exclusively on listed companies. In any case, chapter 9 of the Listing Rules refers to chapter 16 as part of the continuing obligations of listed public companies as a whole.

As a starting point, LR paragraph 16.2 provides that a listed company must ensure that its directors take full responsibility for the company's compliance with the listing rules. Such responsibility is *both individual and collective*. Also, since board personnel have so much influence on the performance of a company as a whole, paragraph 16.3 requires that details of all directors (and, where relevant, senior management) should be included in the company's listing particulars. Subsequently, details of any new directors not included in the listing particulars must be notified to an RIS in accordance with paragraph 16.4.[71] Paragraph 16.7 obliges the company to notify an RIS of any change to the board's composition, such as the appointment, resignation, removal or retirement of any director. In addition, 'changes to any important functions or executive responsibilities of a director' should be notified.[72]

In highly competitive and/or specialised sectors, the relative skills and expertise of company directors can make the difference between relative success and failure. In any case, a company is only as good as its staff and products or services. The board of directors is particularly important, as it determines the focus and strategy of the company. Therefore, any changes in the board's composition must be notified to the market, since it may affect the company's securities, adversely or otherwise. Shareholders will also need to be made aware of such changes, since they might affect the utility of their shareholding, in terms either of voting or even of deciding whether or not to remain a shareholder in that company.

Section 318 of the Companies Act 1985 provides that copies of directors' service contracts having 12 months or more left to run be kept at the company's registered office and made available for inspection by members. This is mirrored in the listing rules at paragraph 16.9, the added layer of obligation (in harmony with the continuing obligations regime generally) being that inspection may be by *any person* and that such service contracts must be at the place of the AGM for at least 15 minutes prior to and during the meeting. Paragraph 16.11 stipulates that such directors' service contracts, as made available, must contain (or have attached to them) a number of specified pieces of information. These, outlined in 16.11(a)–(f), are: the name of the employing company; the date of the contract; the unexpired term and details of any notice periods; full particulars of the director's remuneration, including salary and other benefits; any commission or profit-sharing arrangements; any provision for compensation payable for early termination of the contract; and details of any other arrangements that are necessary to enable investors to estimate the possible liability of the company upon early termination of the contract. Such disclosure requirement as in 16.11 is aimed at presenting full and complete information to a company's shareholders, who in turn can interpret them for their own uses. For example, details of directors' compensation upon early dismissal may influence how shareholders vote in deciding whether or not to terminate a director's service contract.

Some of the most significant provisions of the listing rules relating to directors are in respect of notification of interests of directors and connected persons. Paragraph 16.13 stipulates that:

> 'A company must notify a Regulatory Information Service of . . . any information relating to interests in securities that are, or are to be, listed which is disclosed to the company in accordance with section 324 (duty of director to disclose shareholdings in own company) as extended by section 328 (extension of section 324 to spouses and children) of the Companies Act 1985 or entered in the company's register in accordance with section 325(3) or (4) of that Act.'

This level of disclosure may seem quite intrusive, especially where a director's spouse and children are affected. It must, however, be borne in mind that absent this degree of disclosure, directors could simply purchase multiple batches of securities in the company in the names of their family members and yet totally disguise such potent, if oblique, interests. The latter may, after all, influence a director's judgment in terms of his or her decision making vis-à-vis the company as a whole. The absence of such a disclosure obligation would also allow directors to secretly deal in their company's securities, perhaps on the basis of privileged or inside information.[73] In any event, the proliferation of shareholding in listed public companies further necessitates the availability of as much information as possible about a company and its directors, for the benefit chiefly of the shareholders but also of prospective and potential investors. It is also clear that a director can exercise a considerable degree of direct yet hidden control over the conduct of a company's affairs, depending on the aggregate holding by the director and family members, without it being apparent. Therefore, detailed disclosure of such interests is required, including, *inter alia*, the price, amount and class of securities held. Paragraph 16.13(b) extends this type of disclosure obligation, as part of the continuing obligation, to connected persons.[74] In addition to the items to be disclosed under paragraphs 16.13(a)(i)–(v), the 16.13(b) obligation also requires the disclosure of the identities of the director and the connected person, the nature of their connection, the nature and extent of the director's interest and the particulars outlined in sub-paragraphs (a)(i)–(iv) of paragraph 16.13.

Paragraph 16.13(c) serves as a way of covering the disclosure of all reasonably imaginable eventualities in respect of anything granted to or accepted by a director or a connected person.[75] In essence, any form of right granted to a director (or a connected person) pertaining to any securities of the company must be notified to an RIS. This is to make sure that everything is out in the open and that detailed information is made available to the market. Its merits are twofold. Firstly, it serves as an investor protection mechanism designed to alert the market to possible or potential malpractices by directors, or to any sort of behaviour which may affect the market's dealings with the company and its listed securities. Secondly, the other side of the coin is that it may well serve as a protective mechanism for the directors themselves. The company's disclosure aids transparency, which in turn could aid directors who, in the future, find themselves in some form of controversy regarding interests or dealings in their company's securities. Note that the level of detail required is similar to that required in 16.13(b), and also that notification must be by the end of the business day following the receipt of the information by the company concerned (16.14). The wide scope of the listing rules in this respect is apparent in view of paragraph 16.15, which provides that even a company not subject to the Companies Act 1985 must disclose to an RIS equivalent information to that demanded by paragraph 16.13.

The Model Code

The Appendix to chapter 16, the Model Code, whilst not obligatory for a company is nevertheless expected to be adhered to by listed public companies. This is because, as paragraph 16.19(b) puts it, a company must require adherence by its directors and employees to a code which imposes at least the same degree of strictness as the Model Code. Essentially, this means that, as paragraph 16.19 stipulates, a company may impose more rigorous restrictions on dealings by its directors and employees, but not less. Thus the incentive for companies to impose the provisions of the Model Code is evident.

The Model Code deals with restrictions on dealings in the company's securities by its directors, relevant employees and connected persons, investment managers etc. A regurgitation of all the provisions detailed in the Model Code in this context will serve little purpose to the overall aim of this critical analysis. However, certain provisions are deemed to require brief explanations because of their particular peculiarities and, in any event, the fundamentals are judged worthy of being stated.

Part 3 of the Model Code prohibits a director from dealing in any securities of the listed company during a 'close period'. A close period means a period of two months immediately preceding an announcement or publication of the company's preliminary annual results or of the half-yearly report. In the case of a company reporting on a quarterly basis, the period is one month immediately preceding such an announcement or publication. This is presumably to prevent directors from unfairly benefiting from information that is not yet public by dealings based on it before it reaches the market.

A more significant provision in terms of continuing obligations is contained in paragraph 4, which prohibits a director from dealing in the company's securities at any time when he is in possession of unpublished price-sensitive information (UPSI). The rationale behind this prohibition is self-explanatory, as it serves to prevent insider dealing (which carries criminal liability). Absent this provision, a director may still be liable for insider dealing if successfully prosecuted, but its inclusion provides a clearer and fuller picture for directors. Also, as part of the continuing obligations of a listed company, it serves to remind companies of their duty to take adequate steps to prevent or discourage their employees from engaging in such criminal activity. It is, after all, in the best interests of listed companies that their directors are not found to have been involved in such activities. Perception is critical to the success of companies, particularly those with equity securities listed on a major exchange and so having a multitude of members.

In the event that a director is not in possession of unpublished price-sensitive information, and for the avoidance of doubt as to what constitutes UPSI (notwithstanding its definition in paragraph 1(f)), paragraph 6 prohibits any dealings in the company's securities by a director without prior clearance being obtained from the chairman or other directors designated for such purpose. Paragraph 7 goes on to outline circumstances in which a director must not be given clearance to deal. Paragraph 9 allows clearance to be granted to a director to sell, but not to purchase, securities which he would otherwise have been prohibited from selling, but only in exceptional circumstances such as a pressing financial need that cannot otherwise be satisfied. This denotes a high standard in respect of the threshold to be applied to the definitional interpretation of 'exceptional circumstances'. For the sake of completeness and clarity, paragraphs 19 and 20 outline dealings which are and are not subject to the Model Code, respectively.

Conclusion

Notwithstanding the fact that a company is a legal person — one that may enter into contracts, and may sue and be sued — it is the human personnel charged with its management who actually make decisions and carry out the day-to-day functions of running the business. It is as a result of this inescapable reality that so much significance is afforded to the role of the board of directors. Therefore, issues surrounding changes in board composition affect the integrity of companies and so are required to be notified as part of the continuing obligations regime imposed on listed public companies.

It is also true that directors are decidedly in a position of trust and have the fiduciary duty to perform their duties for the benefit of the company and its members. However, directors who have the dual role of being part of the management as well as the ownership wing of a company have the incentive to act in their own best interest, as opposed to that of the company as a whole. As a result, the relationship between such directors and their companies, in terms of balancing their interests as directors and as shareholders, is closely monitored through provisions aimed at achieving transparency and efficacy of proceedings.

BUY-BACK OF SHARES

Introduction

There are circumstances in which a company may decide to purchase its own securities. Such a purchase by a listed company, whether on or off market, is regulated by the UKLA via chapter 15 of the Listing Rules. Again, transparency of occurrences is the essence of regulation in this context.

As a starting point, paragraph 15.1 states that a company may not purchase its own securities at a time when a director would be prohibited from dealing under the Model Code: for example, during a close period.[76] This effectively equates the level of regulation applicable, via the listing rules at least, to companies with that of directors. The rationale for this seems to be uniformity of rules. Such uniformity is useful in view of the fact that it may be the same director(s) who wish to deal in the company's securities that make the decision as to whether or not to propose a buy-back of the company's securities.

Equity securities: Authority to purchase

Paragraphs 15.3–15.12 apply exclusively to the purchase of a company's own equity shares. 15.3 states that any board proposal to shareholders requesting authority to purchase the company's own equity shares (other than the renewal of an existing authority) must be notified to an RIS. The shareholders' response to the proposal at an AGM should also be disclosed to an RIS immediately. A circular seeking such authority must contain certain details as outlined in paragraph 15.4 and, if it complies, need not be submitted to the UKLA for approval. Paragraph 15.5 adds some extra requirements to be included in the circular in the event that the full exercise of the authority sought would result in the purchase of 15 per cent or more of the company's issued share capital. Paragraph 15.6 stipulates that purchases of less than 15 per cent of any class of equity shares, following a general authority granted by the shareholders, may only be made through the market if the price to be paid is not more than 5 per cent above the average of the market value of those shares for the five business days preceding the purchase.[77]

LR paragraph 15.7 states that purchases of 15 per cent or more of any class of equity shares pursuant to a general shareholder authority must be made by way of either a tender or a partial offer to all shareholders of that class on equal terms. However, where a series of purchases which aggregates to 15 per cent or more of the shares of the relevant class is made following a general shareholder authority, a tender or partial offer need be made only in relation to purchases taking the aggregate amount to or above that level.[78]

LR 15.8 states that a tender offer, if made, must be at a stated maximum price or at a fixed price. Such an offer must be advertised in two national newspapers at least seven days prior to its closing date. This requirement is unnecessary where a circular has been sent to all shareholders in accordance with chapter 15 of the Listing Rules (see 15.4 and 15.5). This is to safeguard the interests of shareholders by giving them sufficient notice that they can make the necessary arrangements for an informed decision: for example, by consulting their financial adviser. The ideal mode of communicating with those shareholders is through a circular detailing the terms and conditions of the offer and other relevant information to aid the investor's decision-making thought process. However, in the absence of such, the company wishing to purchase its own equity securities must still, nevertheless, give significant notice to shareholders by publishing the offer in at least two national newspapers giving members at least seven days' notice.[79]

Holders of convertible securities

A rather strict provision of the listing rules in this respect is the paragraph 15.10 requirement of consent of all the holders of other classes of securities before a company can enter into any buy-back contracts. This is strange in the sense that the company is being obliged to obtain permission from the holders of securities that do not form part of the subject matter of the buy-back. One is, after all, discussing only the purchase of equity shares. Such consent is required of holders of listed securities which are convertible into, exchangeable for or carrying a right to subscribe for equity shares of the class proposed to be purchased. In that case, a separate meeting exclusively of the holders of such securities must be convened so as to seek their approval. An even more incredible development is the fact that in order to maintain such approval the company needs an extraordinary resolution from those securities holders. That is, 75 per cent of those present at the specially convened meeting must support the proposal. It is, therefore, *prima facie*, a contentious requirement of listed public companies.[80]

However, it is also arguable that paragraph 15.10 is still a desirable provision, in that it seeks to protect the underlying quasi-interest of the holders of non-equity shares which are the equity shares in question. That is, the incentive for purchasing, say, convertible shares is that very fact of convertibility into equity (especially voting) shares. The effectuation of such an invasive transaction, affecting the balance and perhaps the value of the company's equity shares, without the knowledge and, most especially, the consent of those holders of securities other than equity shares is unacceptable at best. This is so, as such a share buy-back by the company may well influence those security-holders' decision-making thought processes. For example, they may find the proposed price for the buy-back sufficiently attractive to lead them to exercise their conversion rights earlier than intended, thereby benefiting from the purchase. The conclusion here, therefore, is that the requirement that listed companies obtain such consent from the holders of other relevant or affected securities is a decidedly apt and desirable one.

Conclusion

The regulation of the repurchase of shares by a company is effected in a rather intrusive manner. The listing rules contain specific thresholds in terms of percentages that must be strictly adhered to. It would appear as though the parameters of regulation in this context are almost scientific. As a result, there was considerable engagement with this notion earlier. However, it is submitted that wherever a listed company's financial assets are being extensively utilised by its directors, whether to effect such share buy-backs or otherwise, ample supervision, direct or indirect, should be enforced so as to ensure necessary transparency.

It is considered proper that shareholder consent is sought before any buy-back by the company. A requirement of greater significance, nonetheless, is the 15.3 prerequisite that any board proposal to shareholders requesting their authority to purchase a company's own equity shares (other than the renewal of an existing authority) must be notified to an RIS. The logic to this is that the credibility of the content of such a proposal is safeguarded, as there is less incentive for the board to embellish or indulge in unjustifiable hyperbole. In aid of the provision of full and perfect information to the market, the shareholders' response to such a proposal at an AGM should also be disclosed to an RIS without delay. The rationale for the extension of such consent requirements to holders of convertible securities has been elucidated above. They too should be consulted and their consent sought, provided the proposed purchase affects their underlying equity shares to which their convertibles may be converted.

CONCLUSION

The need for continuing obligations has been articulated as arising out of the need for the law to shield shareholders against possible malpractices by the directors of their listed companies. The increasing relevance of such protection has been exacerbated by the cluster of corporate scandals that have recently been the focus of the news media. The timely dissemination of relevant information to the marketplace as a whole represents the other limb of the rationale for the existence and imposition of those obligations. Furthermore, the underlying principles contained in the Continuing Obligations Guide clearly affirm that the timely disclosure of all relevant information and the equal treatment of all shareholders form the very bedrock of regulation in this area of corporate finance law.

The question of achieving a proper balance between competent regulation of listed public companies and the need to refrain from overburdening boards of directors with regulatory bureaucracy is one that is pertinent to a critical analysis of the continuing obligations regime. This is so as there is a tendency to react to corporate scandals with even more corporate governance provisions. Such knee-jerk reactionary tendencies are bound to face the criticism of failing to be the product of informed scrutiny, as has been alleged in the case of the USA in respect of the Sarbanes-Oxley Act enacted in the aftermath of Enron and other debacles. In relation to the listing rules, such criticism is less potent, especially in view of their EU roots. That is, the fact that they are chiefly the product of well-structured consensual European Directives which have been adopted in the UK, whilst inescapably incorporating the latter's particular idiosyncrasies, means that they are decidedly informed. The continuing obligations which are a part of the listing rules, therefore, enjoy the merits of being informed, whilst the UKLA's guardianship of them also means that they are sufficiently flexible to react quickly to the perpetually changing world around them.

The way forward

In the final analysis, it is submitted, firstly, that the continuing obligations regime imposed on UK-listed public companies and administered by the UKLA is a desirable one. Secondly, it is concluded that that present system, as governed by the listing rules of the UKLA, is sufficiently detailed to effect adequate regulation of listed companies, especially in terms of the proper protection of shareholders and the market. Thirdly, it is conceded that certain requirements (particularly those dealing with public protection) are quite intrusive in nature and so may be frowned upon by companies. However, the nature of the affected companies in terms of their wide assortment of shareholders, as well as the increasingly sophisticated ways in which improprieties (especially those of a financial nature) may be perpetrated, necessitates that such intrusive mechanisms be imposed. Finally, notwithstanding the last point, one must remember that the business of a company is primarily profit maximisation for the benefit of its shareholders, and so the very execution of that role should not be eclipsed or prevented by the imposition of overly stringent rules. That is, proportionality must be maintained to ensure that companies, public or otherwise, are not over-regulated.

The aspiration, conclusively, is that the continuing obligations do not become subject to knee-jerk reactions but instead continue to serve as a functional and valuable contemporary tool of investor/public protection. A point of considerable importance must also, of course, be the maintenance of an adequate balance between the desire for said protection and the need to ensure that companies are not overly discouraged from going public and seeking listing. In addition, there is the pressing need to ensure that knowledgeable experts are not deterred from taking on roles as directors of listed public companies.

References

(1) Such as Enron, Adelphi, Tyco, WorldCom and Maxwell.

(2) The financial aspect of corporate governance. However, the broadness of corporate governance beyond financial matters was evident in Demb and Neubauer's study (*The Corporate Board: Confronting the Paradoxes*) of the operation of boards of directors in eight countries, where they predicted a shift in emphasis in the functions performed by the board from exclusively economic considerations to those dealing with social welfare. Cited by Parkinson in (1995) 'The Role of "Exit" and "Voice" in Corporate Governance', in Sheikh, S. and Rees, W. (eds), *Corporate Governance and Corporate Control*, Cavendish Publishing, ch. 3, at p. 79.

(3) Harris, J. (2002) 'Countering the spread of "Enronitis"', *Company Lawyer*, Vol. 23, No. 4.

(4) *Ibid.* at p. 106.

(5) Chandler, R. and Rees, N. (2002) 'Regulating Company Accounts: All Change Please', *Company Lawyer*, Vol. 23, No. 5, at p. 154.

(6) The UKLA's Guide to the continuing obligations regime, December 2003, Appendix 3.

(7) The Financial Services and Markets Act 2000 (FSMA) confers rule-making powers upon the FSA. As a result of this the FSA has published the Listing Rules, aimed at providing a detailed set of obligations on public companies applicable both when they seek quotation and post-listing.

(8) Note LR chapter 13, which deals with documents not requiring the prior approval of the UKLA.

(9) Keeling, D. (2003) *Corporate Finance: Public Companies and the City*, The College of Law, Jordans.

(10) *Ibid.* at p. 154.

(11) Section 397 *inter alia* renders it a criminal offence for a person to dishonestly conceal any material fact or do any act or engage in any course of conduct which creates a false or misleading impression as to the market in or price or value of any investments.

(12) See para. 9.8.

(13) CA 1985 s. 199(2) states that a member of a company has the obligation to disclose material interests: eg more than 3 per cent of the nominal value of that company's share capital; or where the aggregate nominal value of the shares in which he has interests is equal to or more than 10 per cent of the nominal value of the relevant share capital.

(14) If, following company investigations via a notice requesting details of a person's interests in the company's shares in the three years preceding the date of the notice, such information is discovered, it must be passed on to an RIS.

(15) CA 1985 provides that additional shares of a company must first be offered on a pro-rata basis to the existing shareholders.

(16) Representing 25 per cent or more of the group's aggregate share capital and reserves or profits.

(17) Paragraph 9.35.

(18) Paragraph 9.37.

(19) Paragraph 9.40.

(20) See later section on the buy-back of shares.

(21) Henderson, A. (2003) 'Confident about Confidentiality? Civil Claims for the Misuse of Price Sensitive Information', *Company Lawyer*, Vol. 24, No. 4, at p. 116.

(22) The five class tests are set out in LR para. 10.5.

(23) There are four types of excluded transactions, namely: transactions of a revenue nature in the company's ordinary course of business; an issue of securities or a transaction to raise finance which, in either case, does not involve the acquisition or disposal of any fixed assets of the company; transactions by a company with no equity securities listed; and transactions by an overseas company with a secondary listing by the

UKLA, other than a transaction classified as a reverse takeover.
(24) For better understanding, see *Appendix 3 — Continuing Obligations Guide*, 2003 at p. 27 for an illustration table of the different classifications and the requirements of each.
(25) Note the exception of related-party transactions, which are based not on financial classifications but instead on the relationship between the parties entering into the transaction. The determination of proximity in this respect will be discussed later in this section.
(26) See LR para. 10.5(d).
(27) See LR para. 10.20, which states that the UKLA must be consulted in the event that any of the percentage ratios changes to the extent of altering the classification of a transaction between the time of its first discussion with the UKLA and the announcement.
(28) See LR para. 10.37.
(29) LR para. 10.37 outlines class 1 requirements whilst 10.40 stipulates the detailed required contents of a class 1 circular to shareholders. Extra requirements for class 1 circulars, but specifically in the context of takeovers and mergers, are laid out in 10.45, followed by requirements pertaining to takeovers and mergers generally in paras 10.46–10.50, as well as in the Appendix to chapter 10. Note, also, paras 10.29 and 10.30, which deal with class 3 requirements; and 10.31–10.34, which detail class 2 requirements. In addition, see para. 10.39, which states that following the announcement of an agreed or contemplated reverse takeover the UKLA will suspend listing of the company's securities.
(30) LR para. 11.1(a).
(31) LR para. 11.1(b).
(32) Or a person who was such within the 12 months preceding the date of the transaction: 11.1(b)(ii).
(33) LR para. 11.1(d) and (e) define an associate in respect of individuals and companies respectively. See also para. 11.2 as to multiple related parties.
(34) See also para. 11.5, which states that where a party to the transaction becomes a related party after a circular has been sent out to shareholders, a supplementary circular must be sent out to them detailing the variation.
(35) See LR para. 11.7(a)–(j).
(36) And therefore has only a secondary listing by the UKLA.
(37) That is, transactions where the percentage ratios are equal to or less than 0.25 per cent.
(38) Note, of course, transactions of less than 25 per cent (classes 2 and 3), which are not subject to shareholder voting.
(39) Bagheri, M. (2003) 'Information Intermediaries and the Emergence of the New Financial Regulation Paradigm', *Company Lawyer*, Vol. 24, No. 11, at p. 344.
(40) Harris, J., ref. 3 above, at p. 106.
(41) *Ibid.*
(42) *Ibid.*
(43) See s. 227 CA 1985. Also, Sch. 4A contains details of the form and content of the consolidated accounts.
(44) Sections 235–237 detail the duties of the auditors as well as the required contents of their report.
(45) LR para. 12.42(e). Note s. 244(1) CA 1985 – seven months for public companies, ten months for private companies.
(46) See LR para. 12.43 subparagraphs (b)–(e), (k), (l) and (n)–(v), dealing with such things as commentary on forecasts; directors' interests in shares; details of share buy-back and small related-party transactions. See also para. 12.44 as to 'contracts of significance'.
(47) LR 12.43A(b) further stipulates that the company must state whether or not it has complied, throughout the accounting period in question, with s. 1 of the Combined Code. Where a company has not complied with part or all of the Code, it must specify which provisions of the Code it has not complied with, together with reasons for non-compliance.
(48) That is, its opportunity to raise finance from a broad investor base, plus the fact that those investors are unavoidably diverse.
(49) 1995 SI 1995/2092. Regulation 4 allows a company to send a summary financial statement to an entitled person in place of the copies of its full report and accounts in some instances, eg where the company has ascertained that such a person does not wish to receive copies of those documents. (See also regs 2, 3 and 3A.)
(50) The Takeover Panel, via the City Code on Takeovers and Mergers, also regulates profit forecasts specifically in the context of takeovers and mergers.
(51) Ogowewo, T. (2003) 'Profit Forecasts and the City Code', *Company Lawyer*, Vol. 24, No. 1, at p. 11.
(52) *Ibid.*
(53) Note that Ogowewo's paper treats profit forecasts mainly in the context of takeovers, but the rationale behind regulation as outlined by him is, nevertheless, deemed helpful in this context. The detailed method of regulation by the Panel is, however, beyond the scope of this work.
(54) Ogowewo, T., ref. 51 above, at p. 13.
(55) *Ibid.*
(56) This is required where it is the forecast of an undertaking that is to become a significant part of the issuer's group involved in listing particulars, a class 1 acquisition circular, or any circular containing proposals for shareholders' consideration in respect of the refinancing or reconstruction of the issuer or its group.
(57) The forecast must include a statement of the principal assumptions for each factor that could have a material effect on the achievement of the forecast.
(58) If the results for the period under review differ by 10 per cent or more from any published forecast or estimate by the company for that period, an explanation of the difference must be included in the annual report and accounts.
(59) Keeling, D., ref. 9 above, at p. 160.
(60) Appendix 3 (The Continuing Obligations Guide) December 2003.
(61) *Ibid.* at para. 7.26.
(62) Found mainly in LR ch. 14.
(63) These are scattered around various chapters of the listing rules.
(64) See also para. 14.3, which stipulates that copies of the circular and other relevant materials be supplied to the UKLA.
(65) These must be supplied simultaneously to the UKLA and the shareholders.
(66) Note that LR ch. 13 deals with documents not requiring prior approval. It deals with a lot of non-circular documents, which are in essence beyond the scope of this work.
(67) Included are circulars in respect of the s. 80 authority to allot shares; disapplication of pre-emption rights; notices of meetings; and reminders of conversion rights.
(68) Note, also, para. 10.42, which states that where the listed company is issuing shares for which listing is sought, information regarding major interests in shares, as well as directors' interests in shares, must be disclosed in respect of the share capital both before and after listing. Note that where any such information is contained in the listing particulars, it need not be repeated, as a mere summary will suffice.
(69) For example, with a para. 6.C.20 material contract, or where the related party is a director (or his associate), the circular must include that director's interests in shares (6.F.4 and 6.F.5) and transactions (6.F.6), as well as details of his service contract (6.F.12). Note, also, para. 11.10(d): where a class 1 acquisition or disposal of an asset is involved for

which appropriate financial information is not available, the circular must include an independent valuation. Where an expert's statement is included in a circular not incorporating listing particulars, that circular must state that it is included with the expert's consent.

(70) In addition, para. 15.5 stipulates that where the full exercise of the authority sought would result in the purchase of 15 per cent or more of the company's issued equity shares (excluding treasury shares), the circular must include details of the major interests in shares, significant changes, working capital, name and address of the issuer, directors' interests in shares and group prospects. The para. 15.5 circular must be submitted to the UKLA for prior approval, as 15.4 provides that only circulars not contained in 15.2 or 15.5 need not be submitted for prior approval.

(71) Such notification must be made within 14 days of the director's appointment becoming effective: LR 16.5(b). LR 16.6 simply states that a company must request information from its directors to comply with paragraphs 16.3–16.5. Also, 16.8A adds that where an appointment is made, the notification must specify whether it is an executive or non-executive position and state the nature of any specific function/responsibility of the position.

(72) See para. 16.7(c). Such notification is to be effected without delay and in any event no later than the end of the following business day, but note that no such notification is required where a director retires and is reappointed at an AGM.

(73) Note of course that such actions may amount to the criminal offence of insider dealing under Part V of the Criminal Justice Act 1993, or that of market abuse under s. 118 (Part VIII) of the FSMA 2000.

(74) 'Connected persons' are defined in s. 346 of the Companies Act 1985 and include the director's spouse, child or stepchild, etc.

(75) It includes any option to acquire or dispose of any securities of the company, or any other right or obligation, present or future, conditional or otherwise.

(76) This prohibition does not apply in three circumstances, as outlined in paragraph 15.1(a)–(c):

(i) Company is purchasing securities of a class whose price or value is unlikely to be substantially affected by the publication of the information resulting in the prohibited period.

(ii) The company is purchasing securities in accordance with the term of issue of the securities which have previously been made public (including details of timing and the amount or formula used for price determination).

(iii) The company is purchasing securities in accordance with an agreement where the date, amount and price of the securities to be purchased were fixed at a time when a director of the company would have been free to deal.

(77) Tender and partial offers are exempted from this requirement.

(78) Purchases of own equity shares that have been specifically approved, as opposed to purchases via a general authority, do not count towards the 15 per cent threshold mentioned.

(79) Purchases of a company's own equity shares must be notified to an RIS not later than 7.30 am on the business day following the date of purchase (15.9). Enforcing such market disclosure requirements on the company ensures transparency and availability of sufficient information for potential investors as well. That provision of the Listing Rules goes on to outline the information to be contained in such a disclosure.

(80) Note, though, that such consent is not required where the trust deed or terms of issue of those securities expressly provide for the company to purchase its own equity securities.

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The '287 scam'

A swindle (the '287 scam') which targets the Companies House database in order to defraud companies has been in operation recently. A fraudster uses the internet to obtain details of a particular limited company, including the postal address of its head office and its registered company number. A change of address form 287 is obtained from the Companies House website and a bogus address substituted, which is duly submitted and processed. The fraudster can then open trade accounts and arrange for goods to be delivered at the company's expense to the false address. Companies House does not currently issue a confirmation of address change, so the defrauded company knows nothing of what has happened until evidence of the fraud emerges later.