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# Governance in brief
## Your summary of the latest corporate governance developments

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- Calls for overhaul of the Takeover Code
- ICSA consultation on 'Improving board effectiveness' (Higgs 2)
- New rules on directors remuneration for AIM companies
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### FSA issues tough, new penalty regime

**In Brief:** As part of its ongoing commitment to the principle of credible deterrence, the FSA has issued a new framework for financial penalty setting in relation to market misconduct. The FSA says that the imposition of harder hitting financial penalties which better reflect the scale of a firm's wrongdoing will become a feature of enforcement activity in the future. Under the new framework, fines will be linked more closely to income and be based on:

- up to 20% of a firm's revenue from the product or business area linked to the breach over the relevant period;
- up to 40% of an individual's salary and benefits (including bonuses) from their job relating to the breach in non-market abuse cases; and
- a minimum starting point of £100,000 for individuals in serious market abuse cases.

There is a new and structured five-step penalty setting framework based on three principles of disgorgement, discipline and deterrence and consists of the following steps:

1. removing any profits made from the misconduct;
2. setting a figure to reflect the seriousness of the breach;
3. considering any aggravating and mitigating factors;
4. achieving the appropriate deterrent effect; and
5. applying any settlement discount.

The new penalty regime came into force on 6 March 2010 and applies to any breach which occurs on or after this date.

**Date:** 1 March 2010

**Source:** Financial Services Authority

**Further info:** http://www.fsa.gov.uk/pages/Library/Communication/PR/2010/036.shtml

### Calls for overhaul of the Takeover Code

**In Brief:** Further to the Kraft purchase of Cadbury, Lord Mandelson, the Secretary of State for Business, Innovation and Skills, has called for the takeover rules to be overhauled. Lord Mandelson used his keynote Mansion House speech to the annual trade and industry dinner to set out his recommendations for improvements to the Takeover Code. He believes there is a case for:

- raising the voting threshold for securing a change of ownership to two thirds;
- lowering the requirement for disclosure of share ownership during a bid from 1% to 0.5% so companies can see who is building up stakes on their register;
- giving bidders less time to "put up or shut up" so that the phoney takeover war ends more quickly and properly evidenced bids must be tabled;
- requiring bidders to set out publicly how they intend to finance their bids not just on day one, but over the long term, and their plans for the acquired company, including details of how they intend to make cost savings; and
- requiring greater transparency on advisors' fees and incentives.

Lord Mandelson also called for further consideration on how the statutory duties of company directors should be understood in the fast-moving circumstances of a takeover, when some of the company's newest shareholders may not have a long-term commitment to the company. He believes that we need directors equipped to be stewards rather than just auctioneers and has indicated that he is willing to re-state the Companies Act if that is thought necessary.

The Takeover Panel has taken the decision to consult on the provisions of the Takeover Code. A public consultation paper on these matters will be published as soon as practicable.

**Date:** 24 February 2010

**Source:** The Takeover Panel

**Further info:** http://www.thetakeoverpanel.org.uk/wp-content/uploads/2009/12/2010-6.pdf

http://www.bis.gov.uk/mansion-house-speech

### ICSA consultation on 'Improving board effectiveness' (Higgs 2)

**In Brief:** Improving board effectiveness is the focus of the recent consultation paper from the Institute of Chartered Secretaries and Administrators (ICSA). ICSA has been commissioned by the Financial Reporting Council (FRC) to work with others on its behalf to update as necessary the good practice guidance in the Higgs Guidance, last re-issued in 2006.

The FRC has asked ICSA to consider whether additional guidance should be given on a number of related issues raised in Section A (Leadership) and B (Effectiveness) of the Code. ICSA states that it is clear from the Code review that board effectiveness is considered one of the main drivers of good corporate governance in UK companies. The guidance will seek to help directors and company secretaries understand the issues which need to be thought through and implemented as they aim to deliver the purpose of the Code; and assist stakeholders to appreciate the roles, responsibilities and dynamics of the boards in which they have a strong interest.

The consultation paper identifies five component parts of an effective board and asks whether these are the right areas where guidance could be enhanced and whether there are other areas which the guidance should look at. The five headings are:

- Roles and responsibilities of the board and its members
- Skill levels in the boardroom
- Board decision-making
- The individual on the board
- Accountability

A steering group has been established which includes representatives from the corporates, investors and professional advisers. There will be two consultation stages before completed guidance is submitted to the FRC in October 2010.

**Date:** 2 March 2010

**Deadline for comment:** 16 April 2010

**Source:** The Institute of Chartered Secretaries and Administrators

**Further info:**
http://www.icsa.org.uk/assets/files/pdfs/consultations/ICSA%20Review%20of%20the%20Higgs%20Guidance%20-%20first%20consultation.pdf

**New rules on directors remuneration for AIM companies**

**In Brief:** The London Stock Exchange has issued new disclosure requirements for AIM companies for directors' remuneration which have to be implemented by companies with a financial year end of 31 March 2010 or after.

The amended rules require details of directors' remuneration earned in respect of the financial year by each director of the AIM company acting in such capacity during the financial year. The following items for each director of the AIM company must be provided:

- emoluments and compensation, including any cash or non-cash benefits received;
- share options and other long term incentive plan details, including information on all outstanding options and/or awards; and
- the value of any contributions paid by the AIM company to a pension scheme.

**Date:** 17 February 2010

**Source:** London Stock Exchange

**Further info:**
http://www.londonstockexchange.com/companies-and-advisors/aim/advisers/aim-notices/aim-notice-36.pdf

**HM Treasury moves forward on issuer liability**

**In Brief:** After a period of inactivity whilst officials attempted to deal with the financial crisis, HM Treasury has now moved forward on the subject of issuer liability. In response to stakeholder concerns about the consistency of the new statutory liability regime and whether common law rights of shareholders were at risk, Professor Paul Davies of the London School of Economics was asked to advise on potential changes to ensure that the regime was comprehensive and soundly based. The Government issued a consultation based on Professor Davies' recommendations in July 2008, in which it set out proposals for the extension of the statutory regime for issuer liability. The Government has now responded to the consultation and final Regulations have been laid before Parliament. The Regulations need to be debated in both Houses before they can come into force.

The Regulations extend the liability regime to apply to all information which is published by an issuer by means of a recognised information service, or the availability of which is announced by the issuer by such means. The Regulations set out the circumstances in which an issuer is liable to pay compensation to a person who has acquired, sold or continued to hold securities in reliance on published information to which the Regulations apply and suffered loss as a result of a misstatement or dishonest omission. The issuer is also subject to a new liability for dishonest delay in publishing information.

**Date:** 8 March 2010

**Source:** HM Treasury

**Further info:** http://www.hm-treasury.gov.uk/consult_statutory_regime.htm

**FSA issues final rules on the new listing regime**

**In Brief:** The FSA has published the final stage of its review of the UK Listing Regime. The aim of the review has been to provide greater clarity about the regime's structure and the rights and obligations its creates, so that:

(i) investors will be able to make more informed investment decisions; and

(ii) issuers have appropriate flexibility over the route they wish to pursue to raise capital.

Policy Statement 10/2 confirms the amendments to the Listing Rules which include:

- restructuring the regime into two listing segments – Premium and Standard. Premium denotes the more stringent super-equivalent requirements and Standard is based on EU-minimum standards;
- further sub-dividing these segments into listing categories under which each listed security will be admitted to listing;
- strengthening corporate governance standards for overseas companies; and
- opening the Standard Listing segment to UK companies to provide a level playing field.

The rule changes come into effect on 6 April 2010, except for:

- the requirement for overseas companies with a Premium Listing to offer pre-emption rights to their shareholders, where there is a transitional provision delaying the obligation until after 5 April 2011; and
- a two-year transition, until 31 May 2012, for securities that previously had a Primary Listing but will not qualify for a Premium Listing and will move to a Standard Listing.

**Date:** 26 February 2010

**Source:** Financial Services Authority

**Further info:** http://www.fsa.gov.uk/pages/Library/Policy/Policy/2010/10_02.shtml

### Increased focus by HMRC on gross payments to non-executives

**In Brief:** We are seeing increased focus from HM Revenue & Customs (HMRC) on gross payments to non-executive directors. If companies are making gross payments to non-executive directors there is a high risk of challenge from HMRC as payments should be paid via payroll and subject to appropriate deductions. This applies even where payments are made to the non-executive director via their own personal service company.

In general terms, when any organisation is making payments for an individual's services, it has to consider whether there is a requirement to operate Pay As You Earn (PAYE). In cases where there is a written contract in place between the organisation and a limited company for the provision of the individual, e.g. with an employment agency or a Personal Service Company (PSC), then in the vast majority of cases, there would be no PAYE obligation on the end user (although the agency or the PSC may have a PAYE obligation). However, in relation to a company which is making payments for the services of a director, it is usually the case that the particular individual has been personally appointed as a director. For example, the individual will be named as a statutory director. Experience suggests that usually there will be no written contract in place between the PSC and the company for the provision of services.

HMRC will look at the substance of the arrangement e.g. seeing whether the individual is listed as a director. If this is the case they are likely to maintain that the reality of the arrangement is that the fees are paid as a result of the individual's personal appointment but with an agreement that they will be paid to his PSC. Where there is a direct personal relationship, the directors' fees will be caught by s.62 of the Income Tax (Earnings and Pensions) Act, as income from an "office" and s.6SS of the Social Security Contributions and Benefits Act i.e. 'earnings' for National Insurance contributions (NIC) purposes. This has the consequence that the company making the payments for the directors' services has to account for PAYE and NIC. This is the case even where there is no direct contract between the individual and the company. The company has to determine, based on the facts, whether it has a PAYE and NIC obligation.

**Source:** HM Revenue & Customs

**Further info:** http://www.hmrc.gov.uk/ir35/

### Measuring by halves – Surveying half-yearly financial reporting

**In Brief:** Deloitte's latest survey of half-yearly reporting reports that, overall, the trend seems to be one of continuing improvement as companies become more familiar with the requirements of the Disclosure and Transparency Rules (DTR). The majority of companies in the survey have produced reports with a high level of compliance with the various requirements.

In summary:

- 87% of companies complied with the DTR requirement to disseminate the half-yearly financial report in unedited full text and all reported within the statutory two month deadline:

- 95% of companies included a responsibility statement in their half-yearly results announcements, with 87% including all of the content required by the DTR;

- 21% of companies clearly provided the required information in their interim management reports, an increase from the 10% reported in the previous Deloitte survey 'Our better halves';

- 33% of companies reporting under IFRS 8 met the increased level of segmental analysis required in half-yearly financial reports; and

- the majority of companies applying IFRS 8 for the first time continued to disclose information based on their previously reported segments, with 70% of companies showing no change in either the number of segments or the basis of segmentation.

The publication also includes an illustrative half-yearly report, a disclosure checklist and commentary on current practice.

**Source:** Deloitte

**Further info:** www.deloitte.co.uk/audit

**Time to take action**

- Familiarise the board with the new issuer liability regime.
- Review new listing requirements to determine if any changes to existing arrangements are required.
- Ensure non-executive directors are paid for their services as directors via payroll and subject to appropriate deductions.

**On the horizon**

- FRC revised UK Corporate Governance Code.
- Phase 2 of the review of the Higgs Guidance.

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