Wedlake Bell

IN COUNSEL

WINTER 2018

WELCOME

Welcome to the first edition this year of our In Counsel publication.

Since our Autumn 2017 update there has been a flurry of legal developments affecting your business. We have picked the most interesting and relevant for you. In the corporate world, among others, we comment on the Financial Reporting Council's proposals for refreshing the UK Corporate Governance Code; report on the interesting case of *The Panel on Takeovers and Mergers v David Cunningham King* where the Takeover Panel for the first time applied to court to enforce one of its rulings; and look at ways to resolve shareholder disputes.

In the world of compliance, in order to support you in preparing for the imminent arrival of the General Data Protection Regulation in May of this year, James Castro-Edwards, head of our specialist Data Protection team, and Blair Adams, partner in our Employment team, have prepared a checklist of questions for European HR teams to address in the context of employee data; and Rosalyn Breedy, partner in our Financial Services team, analyses the functions and benefits of Legal Entity Identifiers.

Our Employment team looks at what you can expect in 2018 and provides guidance for employers regarding sexual harassment in the workplace, and our Pensions & Employee Benefits team provides insights into the BT and the GKN pension deficit sagas. Our IP & Commercial team reports on a recent High Court case highlighting the key points of English law to consider regarding joint authorship; and our Property team outlines ways to unlock development sites that are subject to restrictive covenants.

If you would like to know more about any of the topics covered in this update please get in touch.

Wedlake Bell News

We welcome Adam Lynch as a partner in our Corporate & Financial Services Team. Adam joins the firm from Maclay Murray & Spens LLP (now Dentons). His extensive practice spans all aspects of corporate law, from M&A and public company work, through to joint ventures and private equity investments (on both buy-side and sell-side transactions). His client base includes public companies as well as private companies and entrepreneurs. Although Adam advises clients operating within all sectors, he has a specialist focus on the hospitality and leisure and corporate real estate sectors, in which Wedlake Bell has leading expertise and which he will help to develop even further.

Janice Wall, Head of Corporate
Marlies Braun, Editor

CONTENTS

THE NEW UK CORPORATE GOVERNANCE CODE

Edward Craft

The Financial Reporting Council (**FRC**) is the custodian of the UK Corporate Governance Code (the **UK Code**). The FRC needed to refresh the UK Code, and it is now well on the way to doing this. The new UK Code will be shorter and more focussed than before, which is very welcome.

CORPORATE

The UK Code had become rather unwieldy and over-focussed on the trophy issue of remuneration. It had started to lose the intended focus, namely to support and encourage good and effective board room behaviours.

The FRC has done a decent job with its stakeholder management because little in the new document came as a surprise. However, in seeking to be acceptable to a broad constituency, the FRC has not delivered a particularly radical or novel approach. In brief, the new document marks a significant improvement, albeit not without imperfections.

However, there is one critical area where political pressure has been placed on the FRC to use the UK Code to deliver a change which should be delivered through parliament. We have witnessed a lively debate over recent years regarding the duties of directors and to whom these duties should be owed. The UK Code is not the place to set out those duties, and particularly not the place to seek to amend them, but the FRC has sought to do so inserting the two small words "long term" and by stating that part of the functions of a successful board is to "contribute to wider society".

Why is the FRC doing this? It is probably because in these current strange times the government wishes to see changes in governance law and practice but does not wish to dedicate any parliamentary time to achieve such ends.

Let's be clear: we at Wedlake Bell are evangelists of good corporate governance. We firmly believe that, in most cases, the interests of shareholders are best served if the board does have a long-term vision and strategy for the company and remains a good corporate citizen, cognisant of the role the company must play within the community. We work hard to support companies to achieve this. However, the law specifically does not require directors to look to the long term.

The general duty of directors was codified from common law into statute in 2006 and takes the form of section 172 Companies Act 2006. Section 172(1) begins "a director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members and a whole …". This provision was hotly debated in parliament. The words "long term" do not appear. They do, however, appear later in the section, but in a subsidiary manner as one of a number of contributing factors as to how directors should discharge the duty to shareholders, considered alongside the interests of company employees, the need to foster relationships with supplier, customers and others, the impact on the community and the environment, the maintenance of high standard of business reputation and the need to act fairly as between members of a company. The law states that directors must be cognisant of the likely consequences of any decision in the long term, which is not the same as a "long term interest".

The FRC has been put under pressure from the government to make changes to the UK Code to reflect possible evolutions in thinking over the last 12 or so years, which is laudable, save that the UK Code cannot be used as a proxy to the amendment of primary legislation. If, notwithstanding the current parliamentary mathematics, politicians from left and right are of a view that section 172 Companies Act 2006 and the underlying common law from which it was codified should be changed, parliament should legislate accordingly. It is not appropriate for the FRC to deliver what parliament does not wish to deliver itself. The result would be confusion and uncertainty with parliament effectively seeking to abdicate its powers to make law: a highly undesirable result. This presents an important constitutional issue. The FRC should show leadership in the evolution of progressive governance, but must also protect its independence from the changing desires of politicians. Accordingly, we are generally supporting the changes to the UK Code, bar this one.

The consultation runs until 28 February 2018[1] and the objective of the FRC is for the new finalised UK Code to be circulated during the summer, to take effect for financial years commencing on or after 1 February 2019.

For further information please contact Edward Craft at ecraft@wedlakebell.com.

[1] The consultation is available at https://frc.org.uk/consultation-list/2017/consulting-on-a-revised-uk-corporate-governance-co

"SHOULD I STAY OR SHOULD I GO NOW?" – DEALING WITH THE CLASH IN SHAREHOLDER DISPUTES

Edward Starling and Janice Wall

You have sweated blood and tears to build a business from nothing. You have made huge financial and emotional sacrifices to get the business to where it is now. The business is your baby.

And then the divisions start to appear. You want the business to go in different directions. You question your business partner's judgment and morals. You argue. You fall out. The trust is gone.

This is a common scenario. Often it is further complicated by the fact that the business partner is a friend or member of the family. A shareholder dispute becomes like a divorce and emotions run high. It needn't be, but the reality is there is no easy, one size fits all solution.

There are two broad ways to resolve the issues:

1. You come to an agreement; or
2. You are forced to go to court to get a resolution.

Court proceedings are expensive and time consuming and where the parties have a level of interaction, it is always worthwhile exploring a settlement. Sometimes this could be effected through a formal mediation or indeed facilitated discussions. Other times it requires a more formal process to bring the parties to a resolution. The issues below are just some that you should consider when trying to resolve a shareholders dispute where it has reached the stage where the status quo cannot continue.

The Worst Case

If Court proceedings are unavoidable then there are few ways to resolve/determine the issues in court (depending on the circumstances):

1. A claim for a breach of the shareholder agreement (if there is one) or the Company's constitution (although this will not necessarily address the deadlock or future issues);
2. An action to assert that a minority shareholder has been prejudiced by the running of the business by a majority shareholder and an order for purchase/sale of one party's shares; or
3. The company will be wound up by the court – because a deadlock has occurred and there is no other way to resolve the issues and extricate the parties. This is the last resort.

What to think about

The decision making process of how to proceed should involve legal and tax advisors. The approach to the dispute and the resolution to the dispute must be joined up to avoid unintended consequences (and to maximise the efficiency or benefit from the separation). A few key things to consider:

1. What do you want from the situation? Detaching from the emotion, really think about what you want the outcome to be – do you want to try to work it out, do you want to move on, do you want to remain involved, could you have a different but ongoing role, who is actually best to take the business forward?
2. Is the relationship between shareholders sufficient to enable one partner to become a silent or sleeping partner? This would involve one party taking a back seat in the business. It would be prudent to enter a specific shareholders' agreement in order to formalise the relationship and also to ensure the shareholder who remains in the business on a day to day basis is incentivised. A further option may be to consider

changing the shareholder rights or classes of shares given to the remaining or leaving / sleeping shareholder – that usually addresses voting and dividend rights.

3. Could the shareholders bringing in new investors dilute the disputes between the existing shareholders? This may be an attractive way for the shareholders to remain but with third party involvement in the decision making and division of power. However, this may not be appropriate if the underlying issues are only being postponed as opposed to successfully resolved.
4. Where one shareholder is buying out the other, a valuation of the business and shares will need to be agreed. There are a number of ways to value a company and shares so care needs to be taken to try to agree a framework for the valuation. The leaving shareholder may also consider requesting an anti-embarrassment clause to address the risk of the remaining shareholder selling on the shares at a premium shortly after acquisition – these issues should to some extent be addressed in the valuation exercise and in the structure of the consideration (such as deferred consideration / performance related consideration) but this remains very fact specific. The remaining shareholder/company may require restrictive covenants from the leaver not to compete or solicit staff or clients.
5. Is it possible for the company itself to buy back the shares of a leaving shareholder? This may not circumvent some of the relationship issues in the short term but can be perceived a less emotional or personal approach. The same issues of valuation of the shares apply and care needs to be taken by the shareholders (and as directors) to ensure they comply with their obligations in terms of the use of company cash for the purchase and indeed how the use of that cash impacts on future growth plans of the business. This may develop into a more long term purchase plan where the consideration is staggered over a number of years.
6. Tax advice. One of the primary considerations for any exit is tax. Tax advice must be taken to ensure the most tax efficient structure is effected for both the remaining shareholder and the leaver. This may include utilisation of tax exemptions on exit / termination payments, eligibility for entrepreneurs relief and any impact on EIS relief.

It must be remembered that you are discussing a business. The impact on the business of a dispute between its shareholders can itself be catastrophic. There is a real danger that if a commercial attitude (so far as possible in such an emotionally charged situation) is not adopted, the financial implication on the business and the individual shareholders can be very significant. Expectations need to be carefully managed in a situation where, in all likelihood, it will result in neither party being "happy" with the outcome but where a resolution has been found to crystallise the issues and move forward. Save in cases of fraud or blatant wrongdoing by only one party, there will have to be an element of compromise.

….and if you are starting out, enter into a shareholders agreement. It may be a cost to incur at a stage when there is little cash, but it really could save you thousands (and significant management time) further down the line.

For further information please contact Edward Starling at estarling@wedlakebell.com or Janice Wall at jwall@wedlakebell.com

COURT ENFORCES TAKEOVER PANEL RULING

Kate Fleming

CORPORATE

In the recent Court of Session case of *The Panel on Takeovers and Mergers v David Cunningham King*[2], the Takeover Panel for the first time applied to court under section 955 of the Companies Act 2006 (the **Act**) to enforce one of its rulings.

In particular, the Panel made an application for an order requiring Mr King, the chairman of Rangers International Football Club PLC (**Rangers**), to announce and make a mandatory offer of 20p per share for all the issued ordinary share capital of the Rangers not already controlled by himself or his concert parties. This announcement and offer was required to be made within 30 days of the date of the Court's order.

Background

The Takeover Code (the **Code**) applies to takeover and merger transactions of public companies with registered offices in the UK, if any of their securities are admitted to trading on a regulated market or multilateral trading facility such as AIM. The Rangers shares are admitted to trading on AIM.

The proceedings before the Takeover Panel concerned Rule 9.1 of the Code which requires any person, acting alone or in concert, who acquires 30% or more of the voting rights of a company to make an offer to acquire all of the remaining shares.

The proceedings arose out of a series of rulings made by the Executive, the Hearings Committee and the Takeover Appeal Board (**TAB**), all of which found that Mr King had acted in concert with his partners Mr Latham, Mr Taylor and Mr Park in respect of his acquisition of shares in the Rangers which took him over the 30% limit set out in Rule 9.1 of the Code. This meant that the respondent was obliged to make a mandatory offer.

However, the respondent failed to comply with the final TAB decision and did not make the required mandatory offer. As such, the Panel sought a court order under section 995 of the Act to enforce its final ruling.

Questions for the Court

The Court had to consider the following issues:

1. On a proper construction of Section 955 of the Act, what is the ambit of the Court's discretion?
2. If the Court has discretion to refuse an order, should the Court in the exercise of that discretion refuse the order sought by the Panel?

Decision

Construction of section 955 of the Act

Counsel for both parties provided differing interpretations of Section 955 of the Act. Counsel for the Panel was of the view that the section did not give the Court discretion as to whether to make an order but instead only provided limited discretion as to what *type* of order to grant. Counsel for the respondent however was of the view that the Court has discretion as to whether it does or does not pronounce an order.

Based primarily on the wording of the section (in particular, the words 'may make an order'), the Court found in favour of the respondent on this issue and made it clear that the Court has discretion to refuse to grant an order sought under section 955 of the Act. The Court emphasised the fact that the purpose of section 955 is to give the Panel the ability to seek to have its decision enforced but that this does not mean that the Court's role is simply to act as 'a rubber-stamp.'

Should the Court refuse the order sought by the Panel?

Having decided that the Court does have the discretion to refuse to grant an order, the Court next had to decide whether it should exercise such discretion in the circumstances and refuse to grant the order sought by the Panel.

Counsel for the respondent made two submissions to support the argument that the order should be refused:

- **Impecuniosity** – It was submitted that the respondent had insufficient funds to make the offer required under Rule 9 of the Code.
- **Rangers current share price** – It was submitted on behalf of the respondent that if the offer was made at 20p per share, the current Rangers shareholders would not accept it given that this offer was far below the market price of the shares at that time. It was therefore submitted that making an offer would be futile.

Impecuniosity

With regards to the impecuniosity argument, the Court decided that this argument was irrelevant. The respondent was aware that the purchase of the Rangers shares would result in the need to make a mandatory offer in compliance with the Code but proceeded with the purchase in any event. The respondent made the decision to obtain the 30% shareholding in full knowledge of this fact and in full knowledge of his own financial position and how his financial affairs were structured.

[2] **[2017] CSOH 156, 2017**

The Court emphasised the fact that to accept such an argument would 'materially undermine the working of the Panel' as it would in effect allow parties to circumvent Rule 9 of the Code by arranging their financial affairs in such a way so as to enable them to submit that they did not have available funds to comply with Rule 9 if called upon to make a mandatory offer. In any event, the Court also found that, if it was wrong on this point and the impecuniosity argument was relevant, the respondent had, nevertheless, failed to prove his impecuniosity on the evidence submitted.

Rangers share price

With regards to the current Rangers share price argument, the Court found that this was also an irrelevant consideration. In reaching this conclusion, the Court stated that the purpose of the Code was to ensure that shareholders in an offeree company are fairly treated. On this basis, it is not for the respondent to argue at what price an offer should be made nor is it for him to state whether or not the shareholders would accept such an offer. The Court stated that Rule 9 simply requires an offer to be made at a price determined by the provisions of that rule. To accept the relevance of the respondent's arguments would in effect allow 'the party in breach of the rule to decide at what level the offer should be made and beyond that to usurp the position of the shareholders as to whether that offer should be accepted.' This goes against the fundamental nature of the Code itself.

In summary, the Court therefore found in favour of the respondent on the first issue but in respect to the second issue, in favour of the Panel and granted the order sought.

Comment

This case is important as it is the first time the Panel has reverted to the court in order to enforce its rulings rather than rely on the reputational impact of its public censure regime and other traditional sanctions.

It emphasises the courts' powers in enforcing the Panel's decisions but also highlights the fact that the court has the ultimate discretion and the power not to grant an order. Albeit it should be noted that the decision made it clear that the court 'in nearly all cases, if asked by the Panel to enforce its decision by granting an order will do so'.

For further information please contact Kate Fleming at kfleming@wedlakebell.com.

CHANGES TO THE TAKEOVER CODE

Tayne Rankine

Following the consultations in July and September of last year (see our ***Autumn 2017 In Counsel***), the Takeover Panel (the **Panel**) published its response statements on 11 December 2017 along with the changes to the Takeover Code (the **Code**). For the most part, the changes are as originally proposed but with minor amendments following responses received during the consultation process.

The amendments are effective from **8 January 2018** and from that date the Code, as amended, applies to all companies and transactions to which it relates, including transactions on-going as at that date, unless such application would give the amendments retroactive effect.

CORPORATE

Statements of intention

Content requirements

The amendment to Rule 24.2(a)(i) of the Code regarding statements of the offeror's intention remains as proposed in the consultation paper (see "Takeover Code consultation on statements of intention and related matters" ***here***) with one minor change which acknowledges that certain target companies may not have a research and development function. In the offer document, and in addition to stating their intentions and strategic plans with regard to the business, employees and pension schemes of the target, bidders are therefore now required to make specific statements of their intentions with regard to:

- "any research and development functions" of the target (if there are no such functions, a statement to that effect should be made);
- any material change in the balance of the skills and functions of the target's employees and management; and
- the location of the target's headquarters and headquarters functions.

These statements of intention must first be made at the time of the firm offer announcement (allowing more time for stakeholders to consider the offer). Any change of the bidder's intentions during an offer may constitute a material change to information previously disclosed, thus requiring prompt announcement of the new intentions.

Publication of offer document

The amendments to Rules 24.1 and 25.1 as proposed in the consultation have been adopted without change. Thus, under the amended Code, a bidder is now prevented from publishing its offer document until at least 14 days after it makes its firm offer announcement unless it obtains the consent of the target board to a shorter period. Consequently in circumstances of a hostile bid, the target board will have 28 days (instead of 14) from the bidder's firm offer announcement to formulate the opinion and views that it is required to publish in its initial circular in response to the offer.

Post-offer undertakings and post-offer intention statements

The proposed amendments to Rules 19.5 and 19.6 have also been adopted without change. Therefore, bidders and target companies must now publish, among others:

- reports submitted to the Panel regarding post-offer undertakings in all cases, and not only at the discretion of the Panel; and
- where a bidder or target has made post-offer intention statements, at the end of the 12 months from the end of the offer period, a written confirmation of whether or not they have carried out their intentions relating to a particular course of action.

Asset sales

The Code amendments proposed in the consultation paper PCP 2017/1 in relation to asset sales were all adopted as proposed, subject to certain modifications.

Preventing a bidder from circumventing the Code by purchasing significant assets of the target

In order to prevent a bidder from circumventing certain provisions of the Code, the Panel adopted the proposal restricting a bidder from buying assets which are significant in relation to the target instead of acquiring the target company itself. However, taking into account the responses to the consultation, the initial proposal stated in Note 5 on Rule 2.8 was amended so that, in assessing whether assets are significant in relation to the target company, relative values of **75%** (rather than 50% as proposed in the consultation) are typically regarded as significant.

Asset sales and other transactions subject to Rule 21.1

Rule 21.1 (Restrictions on frustrating action) restricts the target board from taking certain actions which might have the effect of frustrating an offer unless the company obtains the prior approval of its shareholders in a general meeting. The amendments make it clear that a target board will not need to obtain shareholder approval under the Code if the proposed action is conditional on the bid being withdrawn or lapsing (although the target board will instead be required to make an announcement of the proposed action).

However, if the target board seeks shareholder approval of a frustrating action in general meeting, it must:

- obtain an independent fairness opinion on the proposed action's financial terms;
- consult the Panel about the proposed shareholder meeting date; and
- send a circular to its shareholders containing specified information.

Furthermore, a new Note on Rule 21.1 was adopted which stipulates the details to be included in the circular or announcement.

Sales of all or substantially all of the target's assets in competition with an offer

The Code, as amended, now contains a new restriction which provides the following: If, in competition with a bid, the target board has agreed to sell all or substantially all of the target's assets and to return to the shareholders all or substantially all of the company's cash balances (including the proceeds of any asset sale), then a statement by the target company quantifying the cash sum expected to be paid to the shareholders will be treated as a "quantified financial benefits statement" which requires approval by the target's accountants and financial advisers and must be accompanied by certain disclosures.

Furthermore, where a company has agreed to sell all or substantially all of the company's assets, the purchaser (or any person acting in concert with the purchaser) of some or all of those assets would only be entitled to buy shares in the target company during the offer period if the price paid per share is not more than the value the target board has stated it expects to return to shareholders pursuant to that asset sale. If the board has stated that the amount to be paid is within a particular range, then the price must not exceed the bottom of the range.

If a target is in an offer period and then begins discussions to sell all or a substantial amount of its assets, any information it provides to the proposed asset purchaser must also be provided to any other offeror or potential offeror.

Setting aside a Rule 2.8 statement

The Panel adopted the proposed Code amendment requiring a bidder making a Rule 2.8 statement (i.e. that it does not intend to go ahead with the proposed bid) to expressly reserve the right to set aside its statement and re-bid for the target, identifying the circumstances in which it will do this.

For further information please contact Tayne Rankine at trankine@wedlakebell.com.

EU SUPPORT FOR SMEs SEEKING TO GROW ON THE CAPITAL MARKETS

Edward Craft

Notwithstanding the stated intention of the UK government to take back control, it remains important to keep abreast of legislative and other initiatives emanating from Brussels. This is because, in a rather strange twist of fate, the current state of sclerosis within the UK legislature and the likelihood of some form of transitional arrangement with the European Union renders it likely that most new UK legislative measures over the next few years will be as a result of EU legislative initiatives, even after Brexit finally takes effect.

The function of the single market, in particular in relation to capital and financial services, was always of great interest to the UK, not least because London has long been, and remains, the EU's dominant market place for such services. The UK was formerly in a position of major influence, with its former Commissioner, Lord Hill, being the European Commissioner responsible for financial stability, financial services and the capital markets union. The UK government gave that up when Lord Hill stepped down in the summer of 2016. However, the capital markets union project continues, even without British leadership.

MIFID II (which was implemented on 3 January 2018) has created the new label of an "SME Growth Market" to encourage the adoption of flexible rules which encourage SME listings and the use of capital markets to fund the development of growth businesses. AIM, the subsidiary market operated by the London Stock Exchange (**LSE**), is by a long way Europe's most successful market for growth companies and the LSE has been successful in getting AIM recognised as the first SME Growth Market, which is great news.

But European markets such as AIM could do better. There remains a dearth of growing European companies seeking to raise equity on the capital markets. Europe is producing only half of the SME IPOs that it generated before the financial crisis (300 on average from 2005-2007, compared with 172 in 2016). In the three years between 2005 and 2007 over EUR 30 billion was raised annually on markets such as AIM at the point of IPO. However, in the much longer eight-year period from 2008 to 2015 less than EUR 23 billion has been raised. The situation is especially acute in certain EU Member States, where mature capital markets do not exist.

The EU wants to see more SMEs using the capital markets across the Union and has launched a consultation on **Building a Proportionate Regulatory Environment to Support SME Listing**. A three-pronged strategy is required:

- making the markets more effective for SMEs;
- supporting SME growth more generally, encouraging these companies to come to the market; and
- using new, nimble and growing companies to create new market demand in those smaller member states which currently struggle to create and maintain public companies.

Capital markets were originally developed to connect capital with businesses which needed it. SMEs are at a stage of operation where equity funding is vital – they often will not be able to satisfy the conditions of banks to receive secured finance. Growing SMEs create new products and jobs and equip us all to face the challenges of the future. Accordingly, any initiative to support the development of risk capital and encourage the supply of companies to the capital markets is to be encouraged.

CORPORATE

Key areas of focus are:

- supporting the pipeline of SMEs seeking to come to the capital markets;
- supporting the professional ecosystems to support companies at IPO stage in many (generally smaller) Member States (note that this is not a major issue in the developed London market);
- increasing institutional and retail investors to hold SME financial instruments, and making the cost of investing and maintaining these proportionate;
- alleviating the administrative and reporting obligations on SMEs whilst maintaining a vibrant market with sufficient and accurate information and ensuring investors remain protected;
- market abuse, transactions with persons discharging management responsibility and insider lists (all under the **Market Abuse Regime**); and
- supporting liquidity for companies on SME Growth Markets.

There is now a broad acceptance that the strict requirements of the EU prospectus regime and other local securities laws have prevented many companies from looking to the capital markets and raising funds outside of a home jurisdiction. After many years of work, in 2017 the EU agreed a new regime which loosened the Prospectus Directive requirements for SMEs. The current initiative seeks to build an ecosystem to support growth SMEs and to further alleviate administrative burdens on them. The alternative is that such companies would otherwise be turned away from European capital markets, into the embrace of private equity or foreign wealth or, alternatively, simply not grow. It is very significant that the EU is acknowledging that it is necessary for the regulatory environment to support SME listings to be "proportionate", striking a balance between investor protection and quality assurance, but without strangling businesses before they can grow.

At the very minimum, the EU is working to highlight the issue and develop an initiative for us all to "get behind growth". We should all work together to deliver more great, innovative European businesses.

The consultation runs until 26 February 2018.[3]

For further information please contact Edward Craft at ecraft@wedlakebell.com.

[3] The consultation is available at https://ec.europa.eu/info/consultations/finance-2017-barriers-listing-smes_en.

LSE'S REVIEW OF THE AIM RULES – FEEDBACK STATEMENT

Edward Craft and Kamalprit Lally

CORPORATE

As reported in our ***Autumn 2017 In Counsel***, in a call for evidence published on 11 July 2017, the London Stock Exchange (**LSE**) sought feedback on certain key areas of the AIM Rules for Companies (the **AIM Rules**) and the AIM Rules for Nominated Advisers.

On 11 December 2017, the LSE published a feedback statement setting out an overview of the responses received and where amendments are proposed:

New early notification process for nominated advisers (nomads) bringing companies to market

Following strong support for this proposal, changes to AIM Rule 2 are proposed to introduce a formal requirement for early notification. Whilst the initial communication will be before the submission of the Schedule One form, its exact timing is to be at the nomad's discretion. The information required to be disclosed is to be published on a template which will be available from the LSE's website. The LSE has made clear, however, that early notification neither diminishes nor substitutes a nomad's obligations to the LSE to be satisfied about an applicant's appropriateness nor the nomad's ongoing obligation to update the LSE on any new information or any changes of circumstances that arise during the admission process.

The benefit of this change is not that there is to be an evaluation of new market entrants, but that the LSE is creating a structure for that. There have been circumstances before where the LSE has not communicated this well and may face claims of caprice. The LSE makes it clear that AIM is its market and no company has a right to be admitted.

LSE guidance on suitability factors

There was overwhelming agreement that providing such guidance would be helpful with respondents stating that increased certainty would be created by providing a set of non-exhaustive examples. Accordingly, a non-exhaustive list is proposed to be incorporated in Schedule Three to the AIM Rules for Nominated Advisers. It should be noted that, simultaneously, changes to AIM Rule nine are also being proposed to emphasise the LSE's discretion to refuse admission. The greater clarity is welcome.

No few float requirement

In its call for evidence, the LSE garnered opinion over whether a free float requirement would be beneficial. The answer was clear: companies and the professional ecosystem around those companies do not want such prescription for a flexible SME growth market.
Whilst the LSE contended that a free float requirement would increase certainty about a company's financial resources and the support of recognised institutions would provide confidence to the wider market about the company's governance and business model, on balance, respondents were not in favour of this proposed change, nor did they support applying a threshold solely to non-revenue generating companies.

New obligation to clearly follow a recognised corporate governance code

The LSE's view is that companies benefit from adopting appropriate governance measures, and recognise that, to be effective, these measures should be tailored to a company's individual requirements and take into account its particular stage of development. Codes provide a helpful point of reference and measurement. The upgrading of the current AIM Rule 26 governance disclosure to a governance requirement was largely supported by respondents who stated that the current principles-based approach provides flexibility and is not disproportionately burdensome or costly, which is a key consideration for small and medium growing companies. A majority of respondents were of the view that it would be beneficial to require AIM companies in their existing AIM Rule 26 disclosures to comply or explain against a recognised industry code, such as the UK Corporate Governance Code, the QCA Code or the AIC Code. Accordingly, AIM Rule 26 is to be upgraded to require up to date 'comply or explain' qualitative disclosures. The codes themselves require annual updating through the corporate governance statement from the company board chair.

Consequential amendments are also being proposed to Schedule One and Schedule Two of the AIM Rules.

Responses to the LSE's conclusions are requested by 29 January 2018.

For further information please contact Edward Craft at ecraft@wedlakebell.com or Kamalprit Lally at klally@wedlakebell.com.

COURT OF APPEAL CLARIFIES SCOPE OF CROSS-BORDER MERGERS REGULATIONS

Marlies Braun

In the recent case of *Easynet Global Services Ltd v Secretary of State for Business, Energy & Industrial Strategy*,[4] one of its first decisions of this year, the Court of Appeal overturned the High Court decision, holding that the proposed merger of several UK companies and one non-UK EEA company into a UK company qualifies as a cross-border merger.

CORPORATE

The proposed merger involved a number of UK companies and a dormant company registered in the Netherlands which had never traded and had no appreciable assets, no relevant liabilities, employees or other obligations (the **Dutch company**) merging with the appellant, Easynet Global Services Ltd. The only purpose of including the Dutch company in the merger proposal was to make it into a cross-border merger within the scope of the Cross-Border Mergers Directive 2005/56/EC (now consolidated into Directive (EU) 2017/1132) (the **Directive**). The Directive is implemented in domestic law by the Companies (Cross-Border Mergers) Regulations 2007 (the **Regulations**).

The High Court in first instance interpreted the Directive and the Regulations in a purposive way, holding that, since the Dutch company had no substance and was only included in the merger proposal in order to engage the Directive and the Regulations, the proposed merger did not fall within the scope of the Directive and the Regulations.[5] It held further that, even if the proposed merger did come within the scope of the Directive and the Regulations, the court would refuse to sanction the merger because this would be "purely as a result of the device of including" the Dutch company.

The Court of Appeal disagreed and allowed the appeal.

Is the proposed merger within the scope of the Directive?

The legal context for the decision of the Court of Appeal is protecting the fundamental *right of freedom of establishment*. Participation in cross-border mergers is a mode of exercise of the right of freedom of establishment and it is the Directive's stated objective to facilitate cross-border mergers.

The Court emphasises that any restriction on the right of freedom of establishment could only arise from the objectives of the Directive to protect the interests of members and others such as creditors, employees and persons dealing with the companies involved in a cross-border merger. Were the UK to make it more difficult to proceed with a cross-border merger where the merger proposal included a subsidiary of a UK company established in another Member State which "had operations which were small in scale or which was dormant", this would constitute a material restriction on the right of freedom of establishment. No such restriction has been stipulated in the Directive or the Regulations.

The Court recognises in particular that cross-border mergers are often undertaken by corporate groups so as to achieve costs savings and to minimise tax liabilities. In such cases, the principle of legal certainty would require a straightforward (rather than purposive) interpretation of the Directive's provisions.

Based on the ordinary meaning of the words used in the relevant provisions, the Court therefore holds that the proposed cross-border merger involving the Dutch company fell within the scope of the Directive and within the definition of "cross-border merger" stated therein. As the Regulations must be interpreted in line with the Directive, the merger also came within the scope of the Regulations.

Does the proposed merger constitute an abuse of law?

The second question before the Court is whether the inclusion of the Dutch company purely in order to take advantage of the cross-border merger procedure of the Directive offends against the principle of abuse of law.

The Court of Appeal does not consider that the inclusion of the Dutch company contravenes the purpose of the Directive. Both sets of rights involved in this case – the right of freedom of establishment and the right of participating in cross-border mergers – have very wide ambits, and the objective of the Directive is, as mentioned above, to facilitate cross-border mergers, for whatever purpose. Accordingly, the Court holds that the proposed merger does not involve an abuse of law.

Comment

The more cumbersome, expensive or restrictive domestic alternatives to the cross-border regime of the Regulations in this case would have been:

i. a scheme of reconstruction under section 900 of the Companies Act 2006 which Easynet did not want to use because of difficulties in relation to transferring contracts from the transferor companies to the transferee company, and
ii. a scheme of reconstruction under section 110 of the Insolvency Act 1986 which would have had tax and reputation disadvantages as compared with the cross-border merger.

This decision will be welcome by international and UK corporate groups operating across Europe and considering group reorganisations as it clarifies that the application of the cross-border regime of the Directive and the Regulations is more widely available.

For further information please contact Marlies Braun at mbraun@wedlakebll.com.

[4] [2018] EWCA Civ 10

[5] *In the matter of Easynet Global Services Limited* [2016] EWHC 2681 (Ch)

CHARITABLE INCORPORATED ORGANISATIONS

Charlotte Barker

A charitable incorporated organisation (**CIO**), being a registered charity, is an alternative legal structure for charities. With effect from 1 January 2018 charitable companies are able to convert to a CIO with a phased implementation time table lasting until August 2018.

Key statutory instruments relating to CIOs which came into force on 1 January 2018 include:

- **The Charites Act 2011 (Commencement No 3) Order 2017 (SI 2017/1230)** – brings into force section 228 to 234 of the Charites Act 2011, which enables charitable companies, registered societies and community interest companies to convert to become charitable incorporated bodies
- **Charitable Incorporated Organisations (Consequential Amendments) Order 2017 (SI 2017/1231)** – amends schedule 6 (Appeals and Applications to Tribunal) of the Charities Act 2011 to enable community interest companies to appeal a decision by the Charity Commission to refuse an application to convert to a CIO and the CIO's registration as a charity.
- **Charitable Incorporated Organisations (Conversion) Regulations 2017 (SI 2017/1232)** – creates a much needed conversion process for the conversion of a community interest company to a CIO and supplements the process already in place for charitable companies to convert to a CIO.
- **Index of Company Names (Listed Bodies) Order 2017 (SI 2017/1233)** – provides for all CIOs (including Scottish CIOs) to be included in the categories of bodies which the registrar of companies at Companies House must maintain in the business name index maintained by Companies House. As such CIOs are required to comply with the rules on the use of sensitive words or expressions in their name.

With its simplified set up process and reduced reporting and accounting requirements a CIO is an attractive alternative to a charitable company and these new rules will be welcomed by those considering setting up or converting to a CIO.

For further information please contact Charlotte Barker at cbarker@wedlakebell.com.

CORPORATE

20 GDPR QUESTIONS FOR EUROPEAN HR TEAMS

James Castro-Edwards and Blair Adams

In many organisations across Europe, HR teams will be integral to GDPR compliance as much of the data affected by the new law will relate to employees.

Time is running out to start the process of ensuring compliance for May 2018, so below we provide a simple checklist of questions to address in the context of employee data:

1. Where is your employee data stored?
2. Are you storing old data that is no longer required?
3. Can you safely destroy or delete it?
4. Who is processing employee data, your organisation or a third party?
5. Do you need to have new agreements with third party service providers (such as payroll, Software as a Service, and data storage) that are GDPR-compliant?
6. Are any of your third party service providers or companies within your corporate group located outside the EU, and if so, do you have a mechanism in place to enable the legal transfer of employee personal data?
7. Why are you storing or processing the data and do you need to continue?
8. Do you have a lawful reason to process the employee data?
9. Do you rely on employees' individual consent for any processing and have you obtained it?
10. Do you need to obtain new or different consent under GDPR?
11. Do you need to put in place privacy statements for existing or new employees?
12. What mechanism or platform will you use to make people aware of privacy statements?
13. What technical and organisational measures (such as layered access policies, staff vetting and data protection training) do you have in place to protect employees' personal data?
14. Do you have a data breach policy?
15. Do you have in place a policy to deal with employee subject access, right to be forgotten requests and other data subject requests under the GDPR?
16. Do you monitor your employees, using CCTV, electronic communications (including social media) and/or systems monitoring, or location tracking, and is your monitoring GDPR-compliant?
17. Do you carry out privacy impact or data protection impact assessments before performing any new data processing operations?
18. Do you maintain a register of your data processing activities?
19. Do you have a data protection officer, or DPO?
20. Are you ready to start?

Wedlake Bell's specialist Employment and Data Protection Teams can help you address these questions in conjunction with our European partner firms.

For further information please contact James Castro-Edwards at jcastro-edwards@wedlakebell.com or Blair Adams at badams@wedlakebell.com.

EMPLOYMENT LAW – HOT TOPICS FOR 2018

Richard Isham and Emily Mathews

2017 saw a number of major themes in employment law: the cancellation of Tribunal fees; the push back against the treatment of individuals engaged in the gig economy; and the fight against sexual harassment. So, what does 2018 have in store?

2018 will see:

- Employment status – potential changes to the legal protections afforded to individuals;
- Mental health and wellbeing – a greater onus on employers to protect workers;
- Technology – the issues that arise as a consequence of the increased use of technology in the workplace;
- Data/data protection – coming into sharper focus, especially with the advent of the GDPR;
- The fight against human trafficking;
- Tax changes in relation to termination payments; and
- Brexit – but this is a topic for another day…

There was a raft of case law in 2017 considering employment status. In *Uber BV v Aslam & Others* the EAT upheld the ET's decision that Uber drivers were workers (to read more on this, ***click here***). Uber's appeal will be heard by the Court of Appeal at some point this year and the Supreme Court is due to hear the appeal in the *Pimlico Plumbers* case in February 2018.

Worker status may be redefined following the recommendations of the Taylor Review and more recently, *"A framework for modern employment"* prepared by the Business Energy and Industrial Strategy Committee. The law needs to be updated to take into account the ever-evolving work arrangements that exist in markets that are transformed by the next "disruptor" business model (often made possible by the power of technology, allowing the use of apps and fuelled by big data).

ACAS has also stimulated the debate in relation to mental health by publishing new Guidance on the promotion of positive mental health in the workplace; done against the backdrop of statistics from the Department of Health that show that one in four of us will experience mental ill health at some points in our lives and ACAS's own statistics that indicate that mental illness costs employers in the UK up to £30 billion per year in lost production, absence from work and recruitment costs. Failure to address mental health issues in the workplace can also put employers at risk of litigation from discrimination claims, unfair dismissal and personal injury claims. The purpose of ACAS's Guidance is to support employers because, if nothing else, it is in their financial interests to improve awareness of mental health issues within their organisations by:

1. tackling the causes of work related mental ill health;
2. creating a culture where staff can talk about their mental health without fear of stigma; and
3. supporting staff members who are experiencing mental ill health.

ACAS's Guidance recommends that businesses create a mental health policy, train managers and educate their workforce so that both physical and mental wellbeing is promoted and supported in the workplace. Our team has been trained in Mental Health First Aid and we have developed an ACAS compliant training and documentation package. If you would like further information, please do get in touch.

ACAS's Guidance comes at a time when technology is also encouraging us to become the most organisationally and personally self-aware of all generations: biometric security for entry systems and authentication for certain areas in the office; sound and motion sensors; air and water quality

control systems; all sorts of sensors to provide information about how our desks, IT equipment, etc. is being used – and all "overseen" by CCTV. As individuals, we also have "fit bits" and other wearable tech that can monitor our exercise, sleep, the air quality of the street and our office environments, as well as water quality. As we continue to own and upgrade personal tech that can tell us about ourselves and our environment, employers will face challenges, including: providing an environment that is both attractive and "fit" to work in; workers who have got not just knowledge of their own physical and mental health, but also of the environment created by their employer, e.g. sick building syndrome, poor light, blurred boundaries between work and home because of tech, leading to lack of rest/the ability to "turn off".

Accordingly, the way that we are classified (employee, worker or independent contractor) affects the rights that we have in the work place; statistics about our susceptibility to mental ill health and the technology that is available to cities, employers and individuals and the personal and sensitive personal data that this personal technology throws off, potentially creates a perfect storm – the contract that individuals work under, the hours that are worked, the ability for the employer to monitor output, the technology that allows cities, employers and individuals to monitor the environmental factors that may impinge upon both physical and mental health, together with the associated data, potentially puts the individual in a very strong position to be able to bring claims concerning their physical and mental wellbeing against those responsible for working conditions and the environment in which work is carried out.

It is for these reasons that we say that 2018 will see a "sea change" in the way that we think about work, our working environment, mental health and wellbeing because the power of existing technology is capable of being utilised to support individuals who claim that, either their physical and/or mental wellbeing is adversely affected by working conditions, including the environment in which they are required to work.

Finally, three further pieces of legislation that will be prominent in 2018:

1. the **Modern Slavery Act 2015**, designed to stem the fastest growing and second most lucrative criminal activity that is human trafficking, will be used more to prosecute those involved in the recruitment, transportation, and harbouring of a person by threat, force, coercion, abduction, deception, or abuse of their vulnerability with the aim of exploiting them;
2. the **General Data Protection Regulation**, otherwise known as the GDPR, is due to come into force as of 25 May 2018. The GDPR will significantly increase the legal obligations on businesses to control, process and protect data in a responsible way. The reputational and financial consequences of failing to comply could be extremely high; and
3. the measures brought in under the **Finance (No.2) Act 2017**, effective from 6 April 2018, that split an employee's termination pay into two types: payments that can still benefit from the £30,000 exemption threshold and those that cannot. Payments up to the £30,000 cap for statutory (and non-contractual and possibly even contractual) redundancy pay remain exempt from both income tax and NICs, as do genuine ex gratia payments, Tribunal awards for wrongful and unfair dismissal, but all PILONs, whether contractual or paid in breach of a contractual right to do so, will be classified as "taxable earnings" and so be subject to both income tax and Class 1 NICs. This change is made in order, it is said, to achieve fairness and clarity – the tax and NICs consequences will be the same for all employees and no longer dependent on how the employment contract is worded or whether termination payments are structured in some other way, such as damages. The foreign service exemption will be abolished too. The tax treatment of compensation for discrimination claims remains dependent on the precise nature of the payment – some will fall within the £30,000 cap (if the discrimination that causes the injury to feelings arises from the termination of the employment) and some will be entirely free of tax and NICs (from 6 April 2018, this will be restricted and apply only in relation to payments in respect of a psychiatric injury or other recognised medical condition). From April 2019, any payment which qualifies for, but is over the £30,000 exemption cap (eg: for loss of office), will become subject to employer's only (not employee's) NICs.

We are here to help, train and advise. We are a business too, so are facing similar challenges – how to be, not just legally compliant, but also ethical, owning a culture that promotes "doing the right thing", but is not naïve and yet is still profitable. If business was easy, we would be out of business.

Happy New Year.

For further information please contact Richard Isham at risham@wedlakebell.com or Emily Mathews at emathews@wedlakebell.com.

SEXUAL HARASSMENT – ISSUES FOR EMPLOYERS

Fiona Rushforth

Sexual harassment has dominated the headlines and social media over past weeks. Now, a new survey by the BBC has confirmed that the issue is not limited to Hollywood: more than half of the women polled stated that they had experienced sexual harassment in the workplace, and one in five men. This follows on from a TUC survey last October, which showed broadly similar results.

Other disturbing statistics reported by a range of surveys are that a high proportion of victims (50-65%) do not report the harassment; and of those that did, a large proportion (40-60%) said that no action was seen to be taken.

Sexual harassment is an issue of great concern for employers. All employers have a duty to protect the health and safety of their staff, including protecting them from sexual harassment. Workers who experience harassment may suffer from stress and absenteeism, or may simply resign.

Companies will also in many cases be legally liable for the harassment of their staff, and for constructive dismissal claims where the employee has resigned. Like all discrimination claims, damages for sexual harassment are uncapped.

Sexual harassment under UK employment law covers a wide range of acts. The legal definition is "unwanted conduct of a sexual nature, that has either the purpose or effect of violating that person's dignity or creating an intimidating, hostile, degrading, humiliating or offensive environment for them." This means that harassment can take place even when there was no negative intention on the part of the harasser, provided the victim's reaction is not unreasonable.

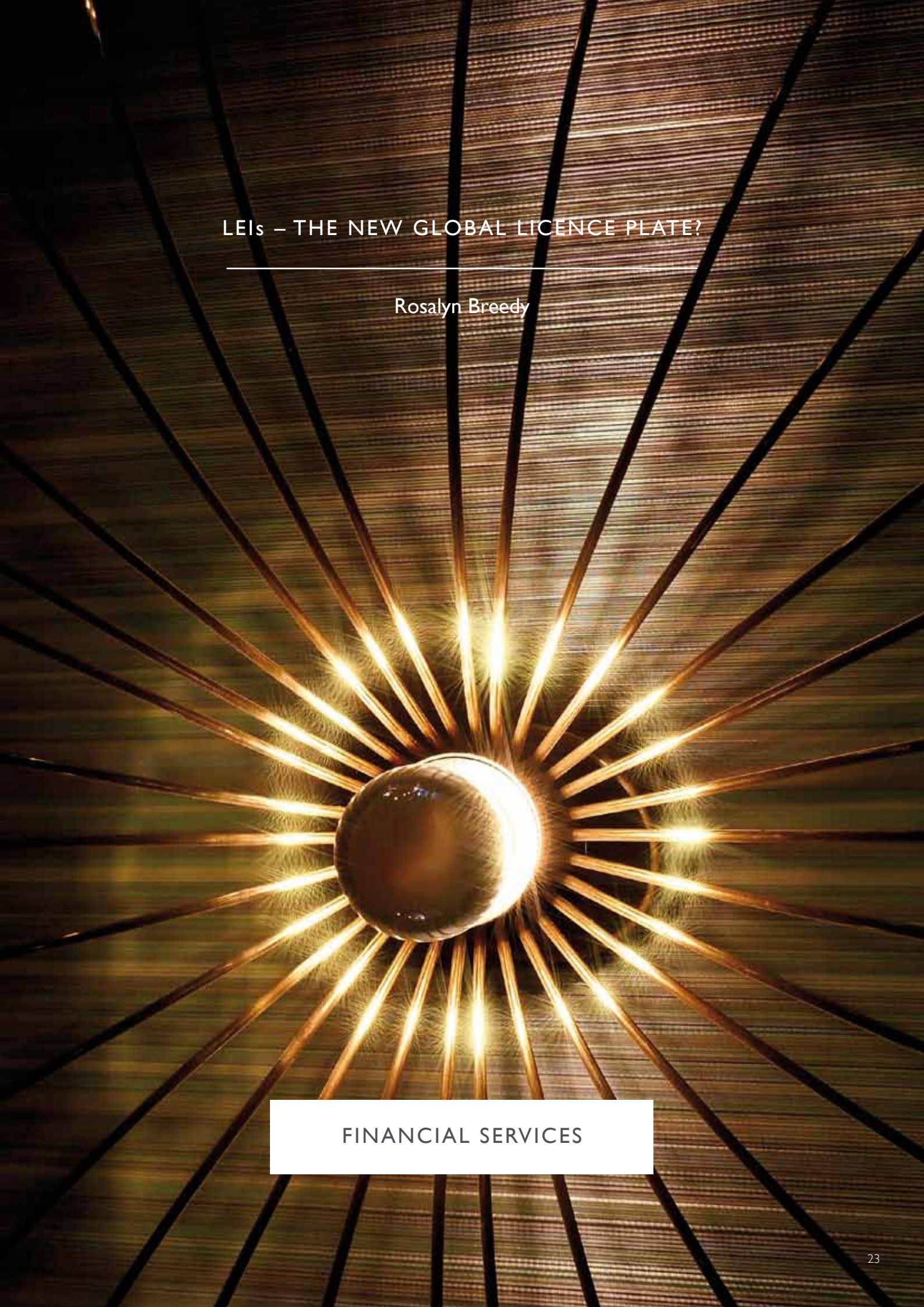
Sexual harassment can include physical conduct or making sexual advances, but also extends to sexual comments, banter, innuendo, or actions such as sharing pornographic images.

Common issues that may arise for employers in the coming months include the following:

- Historic claims: the current public focus on this issue may well mean that employees come forward with allegations of harassment that took place some time ago. In most cases, an employee will not be able to bring an Employment Tribunal claim for harassment that took place more than three months previously. However, it would still be good practice to investigate historic claims and take action if required.
- Avoiding vicarious liability: An employer will have a defence if it can show it took reasonable steps to prevent the harassment. All employees should make sure that they have clear policies and that they actively train staff to promote an environment that does not tolerate any form of harassment. The rules should be made clear, and those who cross the lines should be disciplined or dismissed.
- Harassment outside the workplace: in many cases, the employer will still be liable for harassment that takes place outside work but is linked to their employment, such as a team night out or office party. Companies should make sure that allegations of this type are taken seriously, and that policies make it clear that harassment outside the office will not be tolerated.
- Casuals and agency workers: last year's TUC survey found that low-paid and casual staff, such as those on zero-hours contracts, are particularly vulnerable to harassment. Just like full time and directly employed staff, these workers are entitled to claim against the company if they are harassed by its employees. Employers should ensure that these staff are made aware of the company's policies, and that their complaints are treated seriously.
- #Mentoo – although women make up the majority of complainants, and men the vast majority of harassers, it is worth bearing in mind that allegations by men (including those against women) should be treated equally seriously.

For further information please contact Fiona Rushforth at frushforth@wedlakebell.com.

EMPLOYMENT



LEIs – THE NEW GLOBAL LICENCE PLATE?

Rosalyn Breedy

FINANCIAL SERVICES

"By failing to prepare, you are preparing to fail" – Benjamin Franklin (1709 to 1790).

European banks and brokers may have breathed a sigh of relief over ESMA's Legal Entity Identifier (**LEI**) eleventh hour festive season reprieve a little too early.

The LEI, the global financial services industry's car licence plate, is a 20-digit alpha-numeric code that uniquely identifies legal entities participating in financial transactions.

It was introduced following the 2008 financial crisis because regulators and market participants found that they could not accurately assess counterparty risk.

The complex group structures of some market participants together with differing ways of referring to legal entities meant that it was not easy to understand which legal entities counterparties were dealing with, who those legal entities were owned by and, as a consequence, who owed what to whom.

The Markets in Financial Instruments Regulation (**MiFIR**) which came into force on 3 January 2018 requires EU investment services firms to identify themselves and their clients that are legal persons with LEIs for the purpose of transaction reporting pursuant to MIFID II obligations. This includes firms who execute orders, make the decision to acquire the financial instrument, transmit orders and/or submit transaction reports.

EU trading venues are also required to identify each issuer of a financial instrument traded on their systems with a LEI when making daily data reports to the Financial Instruments Reference Data System (**FIRDS**).

Legal entities, regardless of where they are from, who are clients of an EU investment services firm or are issuers of financial instruments traded on EU markets need to get an LEI regardless of whether they are subject to LEI requirements in their own jurisdictions.

In scope EU investment firms and operators of trading venues are required to have appropriate arrangements in place to collect and verify the LEIs of clients before the transaction takes place.

The ESMA statement was not in fact a reprieve but merely a six month delay with strict conditions. Investment service firms cannot transact for clients without LEIs unless they have obtained in advance the relevant information and make the application for them. Once the LEI is obtained the investment firm will then need to submit its transaction report. The obligation has not gone away.
Trading venues will need to report their own LEI codes instead of the LEI codes of non-EU issuers whilst chivvying non-EU issuers to comply.

LEIs should not be new to in scope firms as they are already required by a host of EU regulations and directives, two of which being the European Markets Infrastructure Regulation (**EMIR**), for counterparties to derivatives contracts as well as beneficiaries, brokers, CCPs and clearing members, and Market Abuse Regulation (**MAR**), for issuers of financial instruments and entities involved in the reporting of suspicious transactions.

LEIs are also required by a number of other international regulations such as Dodd- Frank, where the US have required them since 2012. Other international regulators of mature financial markets such as Hong Kong, Singapore and Canada are also passing regulations requiring their adoption.

The adoption of the LEI is becoming like a vaccine. Unless it is globally adopted across all public financial markets there is a risk of outbreaks of disease. The interdependence of financial markets is elevating the level of adverse impact.

On the positive side, comprehensive adoption of the LEI could potentially be a transformative innovation for financial services allowing the better integration of global markets and a driver to reduce cost.

A recent report by McKinsey & Company highlighted the advantages it could bring to commerce in making more efficient client onboarding processes and in the issuance of letters of credit.[6]

The process of securing a LEI regardless of jurisdiction has also been made easier by the Global Legal Entity Identifier Foundation's (**GLEIF**) introduction of the Registration Agent which helps legal entities access the network of LEI issuing organisations.

The GLEIF is also responsible for the monitoring of the data quality processes and for accrediting the LEI issuers.

Legal entities do not have to use issuers in their own jurisdiction and can use the services of any accredited issuer which is a great boon for multi-national organisations who can use one issuer for their group.

The responsibilities of the legal entity are in fact minimal. The legal entity needs to provide accurate reference information such as the correct legal name and registration number, which the issuer must then cross check with local authoritative sources such as national company registers before issuing an ISO compliant LEI. Changes to data need to be updated and annually renewed.

LEI issuers are obliged to keep fees reasonable and to provide open access because the LEI is seen as a public good.

So banks and brokers need now to use ESMA's six month grace period to apply for LEIs for those clients without them so that business can continue to be transacted smoothly.

Clients, regardless of location of in scope firms who refuse to submit the relevant data, could find themselves shut out of markets as firms choose to turn down business rather than risk contractual liability and enforcement actions for failing to submit compliant transaction reports.

(This article was first published in the *Global Banking & Finance Review* on 18 January 2018 and is reproduced by kind permission.)

For further information please contact Rosalyn Breedy at rbreedy@wedlakebell.com.

[6] The McKinsey report "The legal entity identifier: The value of the unique counterparty ID", Oct 2017, is available at https://www.mckinsey.com/industries/financial-services/our-insights/the-legal-entity-identifier-the-value-of-the-unique-counterparty-id.

IPEC RULES ON THE SKILLS CREATIVES NEED TO DEMONSTRATE TO CLAIM JOINT AUTHORSHIP

Richard Stebbing

Authors, designers or other creatives working together on a project is common-place in many industries. However at what point do these contributions give rise to claims from individuals that, along with the primary author, their contributions make them joint authors of a piece of work?

The recent High Court case of *Martin & Anor v Korgan & Ors*[7] ***(Florence)***, adjudicated on a dispute about the authorship of the screenplay of the film "Florence Foster Jenkins" starring Meryl Streep and Hugh Grant (the **Screenplay**), highlights the key points of English law to consider regarding joint authorship.

Background

The claimants, an established screenplay writer (Mr Martin) and his company, claimed sole authorship of the Screenplay. The defendant (Ms Kogan) claimed joint authorship of the Screenplay.

The first three drafts of the Screenplay were produced whilst Mr Martin and Ms Kogan were living together in a relationship. However this relationship subsequently broke down, meaning that the final version of the Screenplay was produced by Mr Martin without input from Ms Kogan. Ms Kogan's claim of joint authorship centred on aspects of the first three drafts of the Screenplay having survived into the final version of the Screenplay, which she had written herself or on which she had made thematic suggestions to Mr Martin.

The law on joint authorship

Under section 10(1) of the Copyright, Designs and Patents Act 1988, a work of joint authorship is a work produced by the collaboration of two or more authors, in which the contribution of each author is not distinct from that of the other author or authors.

In applying the law to *Florence* the Court considered the following requirements:

1. Was the work produced by a collaboration of two or more authors?
2. Were the contributions of each author distinct?
3. Where a person has contributed to the creation of a work in collaboration with another, is there a sufficient contribution to qualify as a joint author?

The Court's analysis

In relation to Requirement one, the Court noted that the final version of the Screenplay had been produced by Mr Martin after his relationship with Ms Kogan had ended, with evidence showing that the couple were no longer living together and had not discussed the final version of the Screenplay. As such the express requirement that the final version of the Screenplay be produced by a collaboration of two (or more) authors was not met.

Requirement two, which relates to scenarios where distinct pieces of work are published in a compilation, was not in dispute and was not examined in detail by the Court.

In relation to Requirement three, the Court examined whether Ms Kogan's contributions to the previous drafts of the Screenplay were a "sufficient contribution" to qualify her as a joint author.

The significance of the contributions made by Ms Kogan were assessed in relation to the type of skill and labour which she employed, and which would be protected by the copyright in the Screenplay.

Primary and secondary skills

The Court considered a number of authorities relating to what could constitute a "sufficient contribution", providing a useful summary on the relevant case law, dating back to 1921.

The Court considered that, in authoring a piece of work, there is the 'primary skill' of physically creating the work (e.g. holding and using the pen or brush) and the 'secondary skill' of directing the creation of the work (e.g. inventing plot and character, composition, selection of colour). It found that, when considering authorship, the test for demonstrating primary skill is more easily met, meaning that someone looking to rely exclusively on secondary skills would need to demonstrate that he or she had contributed a large amount of secondary skills in order to have made a sufficient contribution to be considered a joint author.

The Court found that secondary skills needed to go to the intellectual creativity of the work, and therefore minor amendments, such as through copywriting, or feedback, which did not create the original work, would not be sufficient.

Summary of factors that are not a "sufficient contribution":

- making contributions, such as scenic effects, that are not subject to the copyright protection afforded to the written material;
- providing expert advice and criticism on the written material;
- providing a highly-technical evaluation of, or 'trouble-shooting', an aspect of the written material; and
- suggesting minor amendments, such as to a stage play script regarding stage direction and presentation.

On the facts Ms Kogan was found to have:

- made some minor plot suggestions;
- provided some technical information to Mr Martin, in relation to musical terminology and history; and
- made some typographical corrections to the first three drafts of the Screenplay.

The Court therefore found that this was not a sufficient contribution for her to be considered a joint author of the Screenplay.

Conclusion

Florence is a helpful authority in summarising the case law on joint authorship and clarifying the threshold for contributors claiming joint authorship through secondary skills.

For creatives looking to collaborate on a project, making the distinction in a design brief between those who will be providing primary and secondary skills in creating a piece of work may be a helpful guide for collaborators on how their contributions will be treated regarding authorship.

The scope of what constitutes secondary skills may be tested in the courts in the future, especially as many of the qualities that fall under 'creative direction' would ordinarily be considered 'ideas' and would not thereby be protected by copyright.

For further information please contact Richard Stebbing at rstebbing@wedlakebell.com.

[7] [2017] EWHC 2927 (IPEC)

BT SET TO "HANG-UP" ON ITS DB PENSION SCHEME

Justin McGilloway

Towards the end of last year BT kicked off a statutory 60 consultation period as part of its proposal to manage its staggering £14bn pension deficit. A consultation document was sent to members of the group's defined benefit pension scheme (the **BTPS**) in November 2017.

This document outlines proposals to:

- close the BTPS to 11,000 BT managers; whilst
- offering continued membership to 21,000 non-managerial BT staff, but with higher member contributions and substantially lower employer contributions.

The main aim of the proposal was to encourage the staff to switch to BT's defined contribution scheme. This is obviously a less generous and riskier alternative for the employees but more affordable for the company. If agreement cannot be reached by next April, BT will close the BTPS to future accrual.

Reaction

As one of the largest pension schemes in the UK, such proposals were never likely to go under the radar. A scheme with assets of over £40bn, 300,000 members and a pending court hearing to consider a change to the inflation measure for pensions in payment coupled with BT being a FTSE 100 company and having a heavily unionised workforce, means that these proposals have been making headlines across tabloids, broadsheets and the internet alike.

The unions are up in arms with some describing the proposals as *"a slap in the face for loyal employees"*. It is fair to state that the unions will play a pivotal role in negotiations with BT during the statutory consultation period (which ended on 17 January 2018) and beyond. The threat of industrial action has been reported by some and of-course this has been used effectively in the public sector over recent years – in relation to many things including pensions. Obviously, the influence of the trade union continues to be strong at BT. Whether the general public will sympathise with the very public plight of the affected employees remains to be seen but for many, this is just another reality of life. Gold plated defined benefit pension schemes were consigned to history for the bulk of the private sector a long time ago!

BT went private over 30 years ago. Since then it has obviously been necessary to keep shareholders happy. It would be an interesting piece of analysis to see how dividends paid out over three decades have compared to the contributions into the BTPS. It is only in the last two years that the UK Pensions Regulator (**TPR**) has expressed its concern over listed companies paying out dividends to the detriment of pension scheme deficits. Earlier this year a representative of TPR stated that:

> *"We are not against companies paying out dividends but employers must strike the right balance between the interests of the scheme and that of its shareholders."*

Furthermore, TPR warned that it was *"likely to intervene"* if it saw a situation where a scheme was *"not being treated fairly"*.

All stakeholders in this saga (BT, the unions and the trustees of the BTPS) will no doubt be well advised as negotiations progress. The press will keep us all updated over the coming months. With changes expected to be implemented one way or another on APRIL FOOLS day this year it is certainly a story that will keep the industry engaged!

For further information please contact Justin McGilloway at jmcgilloway@wedlakebell.com.

GKN OFFER AND THE RESPONSE FROM THE COMPANIES SCHEMES' TRUSTEES

Alison Hills

Final salary funding deficits are all around us and they cause headaches for a number of people, not least:

- pension scheme members who worry about the security of their retirement income;
- employers who have to direct hard earned cash towards schemes to plug significant funding deficits;
- trustees who are responsible for managing poorly funded schemes; and
- investors keen on acquiring companies which happen to be straddled with significant pension scheme liabilities.

The recent bid by Melrose, a mid-cap turnaround company, highlighted several of these headaches when its offer of around £8bn to acquire GKN attracted a very public response from the trustees of the FTSE 100 target's pension schemes. Combined, GKN's schemes have over 32,000 members and a funding deficit, on a gilts flat basis, of £1.1bn. Certainly not sums to be sniffed at.

It appears that the trustees of GKN's schemes got in very early with their warning that the schemes have significant funding liabilities and any potential purchaser needs to be aware of that and have a viable plan to address the issue.

We often hear in the news of parties making significant progress in relation to proposed acquisitions, only for them to fall apart because of the pension deficit. Sainsbury's is a key example of this. In order to avoid this happening it is essential to:

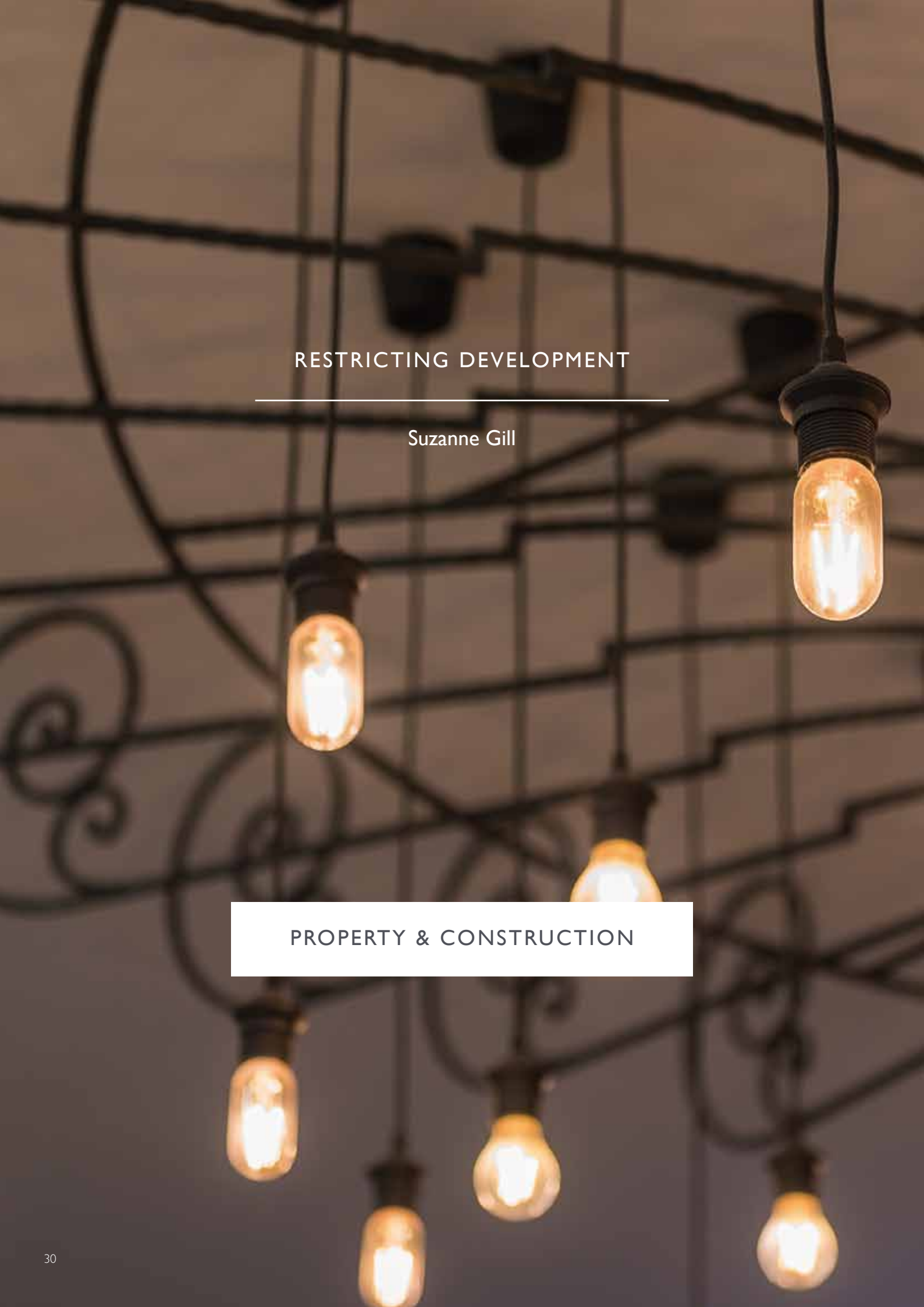
- involve trustees as early as possible; and
- appoint advisers who are going to have a joined-up approach and ensure all potential deal breakers are identified and considered at the outset.

In fact, we are increasingly seeing clients approaching sales/acquisitions with a very clear and logical approach, often considering, at a very early stage, the Takeover Code, applying for Clearance from the Pensions Regulator, and lining up the apportionment of a subsidiary's pension liabilities to another group company before marketing it to prospective buyers, as they are all too aware of the impact a sizable pension deficit can have on prospective sales. Such an approach requires the employer to get the trustees on board and may result in difficult questions regarding employer covenant being raised (something the trustees are obliged to consider as part of their fiduciary duties, and also as a statutory duty in relation to a formal apportionment arrangement). Indeed, covenant is one of the points which the GKN trustees cited as a concern in relation to Melrose's recent offer:

> *"Any material change to the corporate and capital structure of GKN would lead the trustees to reassess the strength of covenant going forward and determine appropriate funding plans based on that covenant and its associated level of risk."*

The GKN trustees appear to be very knowledgeable and proactive. Indeed, if press reports are to be believed, the trustees seem to have a good relationship with the employer and managed to secure £250m worth of funding in 2017 as part of the negotiations surrounding closure to accrual. Melrose have rebuffed the trustees, saying they are aware of the pension liabilities and their offer had taken the liabilities into account, and GNK has said it will instead split itself up and make efforts to improve performance. Splitting itself up may not be the easiest approach though, depending on how the pension liabilities are attributed. We can't help but feel there may be more headlines relating to GKN as 2018 develops.

For further information please contact Alison Hills at ahills@wedlakebell.com.



RESTRICTING DEVELOPMENT

Suzanne Gill

PROPERTY & CONSTRUCTION

It is possible for a landowner to agree to restrict the way in which their land is used (a restrictive covenant), in a manner which lasts for hundreds of years, if it is done properly. Leicester Square remains an open space today because of words drafted in 1808. Sometimes these restrictions are superseded by changes in the neighbourhood: no-one would burn lime or tan leather in central London now.

Sometimes there is a bit of a grey area. Covenants of debatable enforceability can often be dealt with by defective title insurance. Perhaps it is clear that the proposed development will breach a building line shown on an old plan, but there is no one who can complain. Or the title deeds refer to unspecified terms in a deed which has been lost. In these cases, as long as no contact has been made with anyone who might have the benefit of the covenant, it is possible to get defective title insurance for a one-off premium.

However when it is all too clear that the covenant can be enforced, insurance tends not to be available. If negotiation fails, developers have to revise their plans or fall back on an application to the Lands Tribunal. The 1925 Law of Property Act allows for covenants to be modified or discharged in certain circumstances:

- the covenants are obsolete;
- impede a reasonable use of the land; or
- no longer secure any practical benefit.

The process includes writing to everyone who might have the benefit of the covenant alerting them to the hearing, effectively bringing their attention to a right they didn't know they had. No wonder developers treat this as a last resort.

The recent case of *Derreb Limited v Blackheath Cator Estate Residents Limited*[8] concerned covenants which did impede a reasonable use of the land yet at the same time secured continuing practical benefit. How could the Tribunal resolve this dilemma? Derreb owned a former sports ground which was part of the Cator Estate. The property was subject to a restrictive covenant not to build anything other than detached houses on it. Derreb's scheme comprised 38 detached houses – but also 25 terraced houses and 67 apartments. And they had never actually submitted a planning application which was solely for detached houses. Even so, it was clearly in the public interest for a derelict site to be brought back into use. The judges went to the Cator Estate and were struck by its tranquillity and pleasing character, which owed much to the quiet roads and substantial areas of detached housing. These features owed much to the restrictive covenant which was a problem for Derreb.

Tactics and money play an important part in litigation. In this case the developer was the only party to call expert witnesses. Derreb's expert planner maintained that a less intensive scheme would be rejected by the local authority. Furthermore the authority might react by using compulsory purchase powers to acquire the site (thus free from restrictive covenants) and build much more than Derreb proposed. The Tribunal can only make its decision on the evidence presented to it, so these two elements of Derreb's case went unchallenged.

A case report gives only a tantalising glimpse of the legal drama during the hearing itself. This particular judgment makes it clear that the parties (all of them) modified their respective positions during the course of the hearing. By the time the developer's barrister stood up to argue that the covenant was obsolete, two of the objectors had already accepted that some modification of the covenant would be sufficient. It seems that the Tribunal played a more active role in the case than one might expect, perhaps because not all of the objectors were represented by solicitors. In a series of questions the judges prompted the individuals with homes near the site to agree that as long as the part of the development which abutted their homes was of detached dwellings, there would be no damage from flats out of sight; and the residents' company and developer to agree that if the Cator Estate roads were only used by pedestrians, cyclists and mobility vehicles, the character of the Estate would not change. Abolishing the covenants would have meant the residents' only protection against intensive development was the planning process; but amending the covenants was an elegant solution which balanced the rights of all parties involved. Derreb got the rights for a scheme which was pretty close to the one they had asked for, and the residents kept their tranquil low-rise locality.

One of my clients tells me he makes his money on the sites that other people think are too difficult. This case shows how the law can be part of the way to unlock those difficult sites.

For further information please contact Suzanne Gill at sgill@wedlakebell.com.

[8] *Derreb Limited v Blackheath Cator Estate Residents Limited* [2017] UKUT 209 (LC)

STRUCTURALLY SOUND? WOULD A CORPORATE STRUCTURE BE BETTER FOR YOUR PROPERTY DEAL?

Charlotte Barker

PROPERTY & CONSTRUCTION

An alternative to acquiring the direct title to a piece of real estate can be to acquire the corporate vehicle (**Target**) that owns the property. In its simplest terms, this may be done by way of the acquisition of the share capital of an English private limited company, an offshore company or a holding company whose subsidiary owns the real estate in question. By purchasing the shares of the Target, the ownership of the real estate does not change. This can be advantageous when the real estate in question is leasehold property because (unless there are change of control provisions in the relevant lease) landlord's consent will not be required.

Share purchase agreement

Rather than entering into a standard property contract, the parties will enter into a share purchase agreement. The share purchase agreement will be governed by English law, even where the Target is an overseas company holding real estate in England and Wales (although local counsel will be required to opine on certain aspects of the transaction in this instance). Before entering into the formal share purchase agreement, the parties may enter into non-binding heads of terms. The heads of terms may include binding provisions relating to exclusivity and the payment of non-refundable deposits. Unless there is a specific requirement for consent from a third party such as a landlord or regulator, most transactions will be exchanged and completed simultaneously. If a split exchange and completion is required, it is likely that the seller will require the buyer to pay a deposit on exchange that is liable to be forfeited by the buyer in the event that the buyer fails to proceed to completion at the required time. The share purchase agreement will have built into it provisions regarding the conduct of the Target's business during the period between exchange and completion and may give the buyer the ability to terminate the agreement if the seller materially breaches those obligations.

Due diligence

A significant difference to a pure property transaction is that by acquiring ownership of the Target, the buyer also inherits all of the Target's liabilities and history, including tax. As such, in addition to the usual property due diligence that is carried out (including regarding any occupants who will generally retain their right to remain at the property despite the sale), the buyer will need to undertake full legal due diligence on the Target, including financial and tax, so that it can understand exactly what it is buying.

Stamp duty and ATED

Stamp Duty payable on the acquisition of shares in a UK company is 0.5% of the purchase price which is lower than the Stamp Duty Land Tax (**SDLT**) which is payable when the real estate asset itself is purchased – the top rate of SDLT is currently 15% for residential property and 5% for commercial property. Where the transaction is to be structured as a share purchase, in the event that the Target is leveraged with bank debt and/or shareholder loans, the share purchase agreement may be structured so that the debt is discharged by the buyer at completion, with the headline purchase price being reduced by the amount of the debt and thus reducing the level of Stamp Duty to be paid. The consideration may also be subject to a net asset adjustment based on completion accounts, with the adjustments replicating the accruals seen in pure property transactions such as rental receipts and service charge apportionments.

A buyer should also bear in mind that the Target may be liable to pay Annual Tax on Enveloped Dwellings (**ATED**). ATED is an annual tax charge payable by companies that wholly or partly own UK residential property valued over £500,000. Relief from ATED is generally available where the property is let on commercial basis to someone who is unconnected with the company. However, the company will still be required to make annual ATED filings.

A share purchase agreement will not be the right option all of the time, but it is an important structure in the list of possibilities to consider.

For further information please contact Charlotte Barker at cbarker@wedlakebell.com.

CONTRIBUTORS

CORPORATE

JANICE WALL
T: +44 (0)20 7395 3023
E: jwall@wedlakebell.com

EDWARD CRAFT
T: +44 (0)20 7395 3099
E: ecraft@wedlakebell.com

CHARLOTTE BARKER
T: +44 (0)20 7674 0549
E: cbarker@wedlakebell.com

KAMALPRIT LALLY
T: +44 (0)20 7395 3084
E: klally@wedlakebell.com

MARLIES BRAUN
T: +44 (0)20 7395 3184
E: mbraun@wedlakebell.com

KATE FLEMING
T: +44 (0)20 7395 3161
E: kfleming@wedlakebell.com

EMPLOYMENT

BLAIR ADAMS
T: +44 (0)20 7406 1628
E: badams@wedlakebell.com

RICHARD ISHAM
T: +44 (0)20 7395 3133
E: risham@wedlakebell.com

FIONA RUSHFORTH
T: +44 (0)20 7406 1686
E: frushforth@wedlakebell.com

EMILY MATTHEWS
T: +44 (0)20 7395 3042
E: ematthews@wedlakebell.com

DATA PROTECTION

JAMES CASTRO-EDWARDS
T: +44 (0)20 7395 3108
E: jcastro-edwards@wedlakebell.com

FINANCIAL SERVICES

ROSALYN BREEDY
T: +44 (0)20 7406 1629
E: rbreedy@wedlakebell.com

INSOVENCY & RESTRUCTURING

EDWARD STARLING
T: +44 (0)20 7395 3137
E: estarling@wedlakebell.com

IP & COMMERCIAL

RICHARD STEBBING
T: +44 (0)20 7395 3052
E: rstebbing@wedlakebell.com

TAYNE RANKINE
T: +44 (0)20 7395 3182
E: trankine@wedlakebell.com

PENSIONS & EMPLOYEE BENEFITS

JUSTIN MCGILLOWAY
T: +44 (0)20 7395 3076
E: jmcgilloway@wedlakebell.com

ALISON HILLS
T: +44 (0)20 7406 1651
E: ahills@wedlakebell.com

REAL ESTATE & CONSTRUCTION

SUZANNE GILL
T: +44 (0)20 7395 3047
E: sgill@wedlakebell.com

Wedlake Bell LLP
71 Queen Victoria Street, London EC4V 4AY, DX 307441 Cheapside
T: +44 (0)20 7395 3000 | F: +44 (0)20 7395 3100 | E: legal@wedlakebell.com

www.wedlakebell.com