SHEARMAN & STERLING

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GOVERNANCE & SECURITIES LAW FOCUS

Below is a summary of the main developments in US and EU corporate governance and securities law and certain financial markets regulation developments since our last update of October 2017.

The previous quarter's Governance & Securities Law Focus newsletter is available here. Financial regulation developments are available here.

IN THIS ISSUE

EU DEVELOPMENTS

European Commission Publishes Consultation on Institutional Investors and Asset Managers' Duties Regarding Sustainability

On 13 November 2017, the European Commission (**EC**) published a consultation on institutional investors and *asset* managers' duties regarding sustainability. The consultation follows publication of an interim report by the High Level Expert Group on sustainable finance in July 2017, which recommended that the EC clarify that the fiduciary duties of institutional investors and asset managers explicitly integrate material environmental, social and governance factors and long-term sustainability.

The consultation period ran from 13 November 2017 to 22 January 2018 and can be accessed here:

- *https://ec.europa.eu/info/sites/info/files/2017-investors-duties-sustainability-consultation-document_en.pdf*

MAR: Updated ESMA Q&A Includes New Answers on Managers' Transactions and Trading During Closed Periods and on EAMPs

On 21 November 2017, the European Securities and Markets Authority (**ESMA**) published a revised version of its Q&A on the implementation of the Market Abuse Regulation (**MAR**). The new Q&A document includes two new answers on managers' transactions, addressing in particular trading during "closed periods" by persons discharging managerial responsibilities (**PDMRs**) and detailing the types of transactions prohibited during such closed periods.

The updated ESMA MAR Q&A includes a new Question 11 on emission allowances and emission allowances market participants (**EAMPs**). The Q&A is concerned with the time period that should be used to calculate whether one of the emissions thresholds referred to in MAR Article 17.2 has been exceeded so as to bring the EAMP within MAR.

The updated Q&A can be found here:

- *https://www.esma.europa.eu/sites/default/files/library/esma70-145-111_qa_on_mar.pdf*

ESMA Publishes Draft RTS Under the New Prospectus Regulation

On 15 December 2017, ESMA launched a consultation on draft regulatory technical standards (**RTSs**) under the new Prospectus Regulation. The draft RTSs set out requirements in relation to:

- the key financial information that should appear in the summary of the prospectus;
- data for the purposes of classification of a prospectus for ESMA's new online searchable database of approved prospectuses and how to ensure that such data is machine-readable;
- advertisements relating to public offers or admission to trading;
- situations that require the publication of a supplement to a prospectus; and
- publication of a prospectus.

The consultation will end on 9 March 2018, and can be accessed here:

- *https://www.esma.europa.eu/file/24120/download?token=LJOdRdz1*

ESMA Issues Updated Q&A on Alternative Performance Measures Guidelines

On 30 October 2017, ESMA issued a revised version of its Q&A document on the implementation of its Guidelines on Alternative Performance Measures (**APMs**) for listed issuers, adding six new questions and answers.

The new Q&As provide information on areas including: the definition of APMs; the scope of the APM guidelines; how to apply the fair review principle under the APM guidelines; and also how to provide reconciliation between the APM used and the most directly reconcilable line item total or subtotal presented in financial statements.

APMs are financial information on a company's historical or future performance, financial position or cash flow, which are not drawn from the financial statements. The guidelines apply to APMs disclosed by issuers with securities traded on regulated markets, and to persons responsible for drawing up a prospectus.

The revised Q&A document can be found here:

- *https://www.esma.europa.eu/sites/default/files/library/esma32-51-370_qas_on_esma_guidelines_on_apms.pdf*

ESMA Publishes Listed Company Enforcement Priorities for 2017 Financial Statements

On 27 October 2017, ESMA published its annual public statement on European common enforcement priorities for 2017 IFRS financial statements, setting out the priorities that listed companies and their auditors should consider when preparing and auditing their 2017 financial statements. ESMA expects that the statement should help to ensure consistent application of IFRS throughout Europe.

In summary, the 2017 enforcement priorities are as follows:

- Disclosure of the expected impact of major new standards in the period of their initial application – ESMA emphasises the need for high-quality implementation of IFRS 9, *Financial Instruments* and IFRS 15, *Revenue from Contract with Customers* and for enhancing the communication of their expected impact.
- ESMA stresses the importance of the measurement and disclosure of non-performing loans by credit institutions, the ongoing relevance of the fair presentation of financial performance and disclosure on the impact of Brexit. ESMA also emphasises that the 2017 year-end will be the first time that the Accounting Directive (Directive 2013/34/EU, as amended by Directive 2014/95/EU) to disclose non-financial and diversity information will become applicable for certain large groups and undertakings.
- IFRS 3, *Business Combinations* and IAS 7, *Statement of Cash Flows* – ESMA reminds issuers of the continued relevance of the issues that were highlighted in its 2014 Report on IFRS 3, *Business Combinations*, as well as the importance of specific disclosure aspects in relation to IAS 7, *Statement of Cash Flows*.

The full statement can be found here:

- *https://www.esma.europa.eu/sites/default/files/library/esma32-63-340_esma_european_common_enforcement_priorities_2017.pdf*

ESMA Issues Alerts to Firms and Investors on ICOs

ESMA published a statement alerting investors about the high risks of investment in ICOs, including the risk of total loss of their investment.

ICOs are a means of raising money from the public, whereby the issuer issues coins or tokens to be purchased by investors in exchange for traditional currencies or, more often, virtual currencies such as Bitcoin or Ethereum. The coins or tokens are typically created and distributed using distributed ledger technology (**DLT**). In its statement to investors, ESMA cites the key risks of ICOs as: the fact that their structure may mean they are unregulated instruments; some recent ICOs have been fraudulent; ICOs are often used by start-ups with an inherent risk of failure, meaning a high risk of loss of invested capital; it may not be possible to trade the coins or tokens to exit the investment; there is a risk of extreme price volatility;

information provided to investors can be limited; and the DLT technology underpinning ICOs is largely untested and may therefore potentially contain flaws.

- *View the Alert to Investors*.

European Commission Consults on Improving the SME Markets

The European Commission published a consultation paper in which it seeks views on the main challenges for SME-dedicated markets and possible changes to EU legislation that might help build the EU high-growth SME markets. The consultation paper follows previous consultations and papers relating to the Capital Markets Union Action Plan.

The consultation focuses on SME Growth Markets, a new type of trading venue introduced under the Markets in Financial Instruments package (**MiFID II**). The consultation paper is split into two sections, the first of which considers the main drivers behind the downward trend of SME initial public offerings and bond issuances. The second section considers specific regulatory barriers to SME markets, small issuers and the local ecosystems surrounding SME markets. In particular, the Commission is seeking views on the MiFID II provisions which set the scope of SME Growth Markets, the market requirements for SME issuers to be assisted by a key adviser, delisting rules on SME Growth Markets and transfer of listings.

In addition, the consultation paper considers whether steps can be taken to alleviate the administrative burden on SME Growth Market issuers, including assessing some of the requirements in MAR relating to management transactions, insider lists, disclosure of inside information, reporting obligations and market soundings. The discussion on the local ecosystems around SME Growth Markets focuses on the "tick size" regime under MiFID II, the possibility of creating a liquidity provision contract across the EU (as an accepted market practice under MAR). It also covers the merits, if any, of free float requirements for SMEs, regulatory barriers to institutional investments in SME shares or bonds listed on SME Growth Markets and credit assessments and ratings for SME bond issuers.

Responses to the consultation are requested by 26 February 2018.

- *View the consultation paper*.

European Parliament and Council Reach Agreement on Proposal to Amend Fourth Anti-Money Laundering Directive

On 15 December 2017, the EC announced that the European Parliament and the Council of the European Union had reached political agreement on the Commission's proposal to amend the Fourth Anti-Money Laundering Directive (**4AMLD**).

The proposed changes include:

- compulsory disclosure of certain information on beneficial owners of companies and business-related trusts;
- improved access to beneficial ownership information;
- requirement to identify beneficial owners who hold 10% ownership in certain companies which present a specific risk of being used for money laundering and tax evasion (the current threshold level for these purposes is 25%); and
- direct interconnection of national beneficial ownership registries.

On 19 December 2017, the political agreement between the Council of the European Union and the European Parliament on the draft text of the proposed Fifth Anti-Money Laundering Directive (**5AMLD**) was announced.

The 5AMLD can be accessed in full here:

- *http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CONSIL:ST_15849_2017_INIT&from=EN*

UK DEVELOPMENTS

Scottish Court of Session Grants Order Requiring Individual to Make Rule 9 Mandatory Offer

On 22 December 2017, in the decision of *The Panel on Takeovers and Mergers v David Cunningham King [2017] CSOH 156*, the court considered a situation where a shareholder had, acting in concert with other parties, acquired interests in shares carrying more than 30% of the voting rights in a company. This triggered an obligation under Rule 9.1 of the Takeover Code (the "Code") to extend an offer to acquire the shares of the company's other shareholders on the terms stipulated by Rules 9.3 and 9.5 of the Code. The individual did not make this offer, and the Panel initiated proceedings with the Scottish Court of Session seeking an order for compliance with the ruling.

The court considered two questions:

- Did the court have discretion to decide whether or not to grant an order to enforce compliance with the Code?
  - It was concluded that the court does have discretion to refuse to grant an order in these circumstances.
- If the court has discretion to refuse the order, should the court in the exercise of that discretion refuse the order sought?
  - It was held that the court should not refuse the order but should exercise its discretion in favour of granting the order sought by the Panel and obliging the individual to make the Rule 9 mandatory offer.

The financial circumstances of the individual and the fact that the mandatory offer price was significantly lower than the current share price were irrelevant considerations for the purposes of the court's exercise of the discretion to grant the order.

The decision can be read in full here:

- *http://www.bailii.org/scot/cases/ScotCS/2017/%5b2017%5d_CSOH_156.html*

Joint Money Laundering Steer Group Publishes Finalised Revised AML Guidance

On 21 December 2017, the Joint Money Laundering Steer Group published a revised version of its Guidance on the prevention of money laundering and the financing of terrorism for the U.K. financial services industry. This follows feedback to its November 2017 consultation on proposed amendments to its June 2017 Guidance.

Although the amended Guidance will only take over the "legal" status of the existing Guidance once it has been approved by a Treasury Minister, firms are free to use the provisions of the new Guidance immediately, if they wish to do so.

The current Guidance can be accessed here:

- *Guidance Part I*
- *Guidance Part II*
- *Guidance Part III*

Investment Association Launches Public Register of Listed Companies Which Have Had Significant Shareholder Rebellions

On 19 December 2017, the Investment Association (**IA**) announced that it launched the word's first public register of listed companies that have had significant shareholder rebellions. This public register was proposed in response to the green paper on corporate governance reform produced by the Department for Business, Energy and Industrial Strategy in November 2016.

The register details the names of listed companies who encounter shareholder opposition of 20% or more to pay awards and other resolutions, along with a record of what these companies say they are doing to address shareholder concerns. The IA also wrote to companies on the public register in October 2017, giving them an opportunity to provide a public explanation of how they have addressed any shareholder concerns prior to the public register going live.

The public register can be accessed here:

- *https://www.theinvestmentassociation.org/publicregister.html*

FRC Publishes First Audit and Assurance Lab Report

On 18 December 2017, the Financial Reporting Council (the "**FRC**") announced publication of its pilot Audit & Assurance Lab report. The report is a pilot project of the FRC's Audit and Assurance Lab, which encourages audit committees, companies, investors and auditors to collaborate on best practice on audit related issues.

The report highlights that investors particularly look to the audit committee to give them confidence in the appointment of the external auditor, to monitor the auditor's independence and objectivity and promote audit quality.

The report can be accessed here:

- *https://frc.org.uk/getattachment/7f97f065-d912-4ca0-a96b-1f2fd4b0a565/LAB_Final.pdf*

FRC Publishes Revised Guidance for Auditors When Agreeing to the Publication of Preliminary Announcements

On 15 December 2017, the FRC published a bulletin entitled "*The Auditor's Association with Preliminary Announcements made in accordance with U.K. Listing Rules.*" This contains revised guidance for auditors when agreeing to the publication of preliminary announcements.

The purpose of the new report is to provide investors with greater transparency about the status of the information included within the preliminary announcements. Whereas most premium listed companies in the United Kingdom base their preliminary announcements on audited information, the guidance also deals with situations where the auditor is asked to agree on the publication of an "unaudited" preliminary announcement.

The guidance can be accessed here:

- *https://www.frc.org.uk/document-library/audit-and-assurance/2017/bulletin-the-auditor-s-association-with-prelimin*

FRC Publishes Report on Digital Future of Corporate Reporting

On 13 December 2017, the FRC's Financial Reporting Lab announced publication of its report on the digital future of corporate reporting. The report focuses on how corporate reporting might be optimised using technology, demonstrating a move away from paper-based annual reporting.

The report provides a summary of the potential impacts and issues of the use of eXtensible Business Reporting Language (**XBLR**) and concludes that it is an important technology in the path to digitisation of company reporting. With the goal of fully realising the potential of XBRL and responding to the challenge of a new European Single Electronic Format for digital corporate reporting due in 2020, the Lab recommends a series of actions for regulators, technology companies, preparers (listed companies) and investors.

The report can be accessed here:

- *https://frc.org.uk/getattachment/9279091c-a4e9-4389-bdd6-d8dc5563b14a/DigFutureXBRLDec.pdf*

FRC Publishes Revised UK Corporate Governance Code for Consultation

On 5 December 2017, the FRC published for consultation proposed revisions to the U.K. Corporate Governance Code (**UKCGC**) and Guidance on Board Effectiveness. The closing date for responses to the consultation is 28 February 2018. Following consideration of responses to the consultation, the FRC is aiming to publish a final version of the new UKCGC by early summer 2018, with the expectation that it will apply to accounting periods beginning on or after 1 January 2019.

Some of the key changes are as follows:

- The FRC states that the revised UKCGC is "...shorter and sharper...," comprising 17 Principles and 41 Provisions divided into five sections. The new Principles and Provisions are intended to address the elements of governance most important to board effectiveness and corporate purpose, and to focus on stakeholders (rather than just shareholders), integrity and corporate culture, diversity and how the overall governance of the company contributes to its long-term success.
- The "comply or explain" principle is preserved.
- There is a new UKCGC Principle emphasising the importance of the intrinsic value of corporate culture.
- Provision 6 sets out the requirement that where more than 20% of votes have been cast against a resolution, the company must explain what actions it intends to take to consult with shareholders to understand this vote. The company must provide a further update six months later and a final summary in the annual report. Please see "*Investment Association Launches Public Register of Listed Companies Which Have Had Significant Shareholder Rebellions*" above for details of the public register of this information that the IA will keep.
- Principle J aims to broaden boards' perception of diversity and ensure appointment and succession planning are designed to promote diversity of gender and social and ethnic backgrounds. Provision 23 encourages reporting on such actions.
- The Hampton-Alexander Review recommended that the UKCGC be revised to require that FTSE 350 companies disclose in their annual report the gender balance on their Executive Committee. The FRC proposes to extend this requirement to companies outside the FTSE 350 as well.
- The FRC has also provided revised Guidance on Board Effectiveness. It anticipates further changes in response to the results of the UKCGC consultation.

The proposed revisions can be found here:

- *https://frc.org.uk/getattachment/bff48ee6-4fce-4593-9768-77914dbf0b86/Proposed-Revisions-to-the-UK-Corporate-Governance-Code-Appendix-A-Dec-2017.pdf*

IA Issues Position Paper on Virtual-Only AGMs

On 17 December 2017, the IA issued a position paper, which sets out the views of its members on virtual-only annual general meetings (**AGMs**).

The position paper sets out the view of the IA that, although technology is useful to complement the physical AGM, companies should not adopt a "virtual-only" approach. The IA states that virtual-only AGMs remove the public accountability of board members due to the remoteness of participants, whilst physical meetings demonstrate commitment to understanding the views of shareholders.

The IA concluded that its members will not support amendments to the Articles of Association of companies in relation to electronic meetings if they allow for virtual-only AGMs. They expect any amendments to the Articles of Association to confirm that a physical meeting will be held alongside an electronic element.

The position paper can be accessed here:

- *https://www.theinvestmentassociation.org/assets/files/ivis/20171211%20-%20CG-%20Virtual%20AGMs%20IA%20position%20statement.pdf*

LSE Summarizes 2017 Enforcement Actions for Breaches of AIM Rules and Nomad Rules

On 14 December 2017, the London Stock Exchange (**LSE**) issued an AIM Disciplinary Notice (**AD17**) which sets out a summary of enforcement matters which resulted in private censures and fines on AIM companies and nominated advisers ("**Nomads**") during 2017. AD17 is intended to provide guidance to AIM companies and Nomads on the expected standards of conduct to avoid future fines or censures.

The AIM disciplinary notice can be accessed here:

- *http://www.londonstockexchange.com/companies-and-advisors/aim/advisers/aim-notices/ad17.pdf*

FCA Imposes First Fine on AIM Company for Late Disclosure Under MAR

On 14 December 2017, the FCA announced that it had fined an AIM company for failing to inform the market of inside information as required by Article 17(1) of MAR.

The company in question failed to inform the public as soon as possible after being notified that there was a reasonable expectation that it would be required to sell one of its two material investments for no initial consideration, with only a possibility of receiving deferred consideration that was materially lower than the company's valuation of its investment. The failure to disclose inside information prevented investors from making fully informed investment decisions.

The breach arose because of a misunderstanding of the legal effect of a share purchase agreement. The FCA commented that issuers "must have regard to their disclosure obligations at all times and misunderstanding the commercial reality of a transaction is no excuse."

The FCA announcement can be accessed here:

- *https://www.fca.org.uk/news/press-releases/aim-investment-company-fined-failing-disclose-inside-information-soon-possible*

FCA Publishes Market Watch No. 55

On 12 December 2017, the FCA published Market Watch No. 55 newsletter, covering issues regarding current market conduct and transaction reporting issues.

The newsletter addresses the following points, amongst others:

- the transaction reports of an investment firm in a chain should accurately reflect the transaction from the investment firm's own perspective and report its immediate counterparty or client (unless it meets the transmission conditions under Article 4 of Commission Delegated Regulation (EU) 2017/590;

- investment firms have an obligation to transaction report as quickly as possible and no later than the close of the working day following the day that the transaction took place;
- from January 2018, where an emission allowance market participant (**EAMP**) has delayed the disclosure of inside information in accordance with MAR Article 17, the EAMP must notify the FCA of the delay immediately after the disclosure of this information; and
- PDMRs within EAMPs and within parties involved in relevant auctions and persons closely associated with them, are required under MAR Article 19 to notify the EAMPs or the parties involved in relevant auctions and the FCA of transactions conducted on their own account relating to emission allowances, auction products based on them or derivates related to them, if the total amount of transactions per calendar year has reached EUR 5,000.

The newsletter can be accessed here:

- *https://www.fca.org.uk/publication/newsletters/market-watch-55.pdf*

FCA Issues Quarterly Consultation Paper on FCA Handbook Amendments

On 1 December 2017, the FCA issued a Quarterly Consultation Paper 19 (CP 17/39), which consults on proposed miscellaneous amendments to the FCA Handbook. The consultation is aimed at any firm that has an interest in the subject matter of the following proposals, amongst others:

- proposed changes to the regulatory reporting requirements;
- proposed changes to the guidance notes on the completion of the Annual Financial Crime Report to reflect changes in the Money Launder, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (**MLRs**); and
- proposed changes to the Listing Rules to clarify the meaning of Premium Listing Principle 6, and to clarify where diversity reporting may be located under corporate governance reporting requirements in the Disclosure and Transparency Rules (**DTR**).

The FCA Handbook can be accessed here:

- *https://www.fca.org.uk/publication/consultation/cp17-39.pdf*

The consultation paper can be accessed here:

- *https://www.handbook.fca.org.uk/handbook*

FCA Publishes Market Watch No. 54

On 8 November 2017, the FCA published Market Watch No. 54, which covers issues regarding current market conduct and transaction reporting. Included in the review is a reminder for firms with transaction reporting obligations to make sure they have a LEI and to keep it updated. It also reminds charities and trusts, and others not directly subject to reporting requirements, that, from 3 January 2018, they will need to make arrangements to obtain a LEI Code if they want an executing firm to continue to act on their instructions.

Market Watch No. 54 can be found here:

- *https://www.fca.org.uk/publication/newsletters/market-watch-54.pdf*

Changes to the Code and New Practice Statement No. 32

In the October 2017 edition of *Governance & Securities Law Focus*, we discussed certain proposed changes to the Code that the U.K. Takeover Panel (the "**Panel**") was consulting on, with respect to, among other things:

- Stopping a bidder circumventing restrictions under the Code that would prevent it making or varying an offer, by instead purchasing "significant assets" of the target.
- Where a target, in competition with a takeover offer for it, has agreed to the sale of all or substantially all of its assets:
  - requiring the target to make greater disclosure about any statements that it makes about the cash sum it would propose to return to shareholders as a result of the asset sale; and
  - restricting a purchaser of those assets from acquiring shares in the target in certain circumstances.
- Requiring greater disclosure about transactions by targets which take place during offer periods (or when an offer may be imminent).
- Requiring greater disclosure by bidders of their future intentions with regard to the target and its operations, and requiring this to be made earlier in the bid process.
- Unless the target agrees otherwise, requiring a bidder to delay by 14 days the posting of its offer document following the announcement of its firm intention to make an offer.

On 11 December 2017, the Panel announced that it would be proceeding with these proposed changes with few relatively minor revisions to them and that they would take effect on 8 January 2018.

The Panel also announced the issue of a new Practice Statement (No. 32) dealing with the question of when a target will no longer be subject to the restrictions and prohibitions under Rule 21.1 of the Code on it taking potentially "frustrating action" (*e.g.*, an asset disposal or acquisition) with respect to a potential bid. Practice Statements provide informal guidance as to how the Panel interprets and applies relevant provisions of the Code but are not binding on the Panel.

Our client publication about these changes to the Code and the new Practice Statement can be accessed here:

- *http://www.shearman.com/en/newsinsights/publications/2018/01/changes-uk-code-asset-sales-and-other*

LSE Publishes Feedback and Consultation on Review of AIM Rules

On 11 July 2017, via AIM Notice 46, the LSE issued a discussion paper to invite feedback on various areas of the AIM Rules for Companies and AIM rules for nomads. On 11 December 2017, the LSE published AIM Notice 49, attached to which is LSE's Feedback Statement and Consultation in relation to proposed changes to the AIM Rules for Companies and the AIM rules for nomads ("**AIM Rulebooks**").

The feedback statement provides an overview of the responses received, and, where the LSE is proposing to make amendments to the AIM Rulebooks, proposals for consultation.

The consultation closing date is 29 January 2018. The feedback statement and consultation can be accessed here:

- *http://www.londonstockexchange.com/companies-and-advisors/aim/advisers/aim-notices/feedback-statement-and-consultation.pdf*

LSE Publishes Notice on Application for SME Growth Market Status

On 5 December 2017, the LSE published AIM Notice 48 on the application for AIM to be registered as an "SME Growth Market" and minor consequential amendments to the AIM Rules for companies.

The notice states that, from 3 January 2018, MiFID II will introduce a new designation of SME Growth Market, which operators of qualifying markets can voluntarily apply for. The SME Growth Market designation has been developed by the EC as part of its capital markets union plan to create a bespoke regulatory framework for European growth markets. The designation is also expected to raise the profile and visibility of SME Growth Markets across the EU and distinguish them from multilateral trading facilities, which generally operate as trading facilities that do not have a primary market function.

The LSE received final approval regarding this application, and it took effect from 3 January 2018. To meet the necessary requirements, there have been some minor amendments to the AIM Rules. For instance, AIM Rule 26 (Company information disclosure) has been amended to reflect the requirement that certain regulatory information must remain available for five years once published under Article 78(2)(i) of Commission Delegated Regulation (2017/565/EU). As such, prospectuses, annual accounts and inside information (among others) will need to be maintained on the AIM company's website for at least five years, once published.

The notice can be found here:

- *http://www.londonstockexchange.com/companies-and-advisors/aim/advisers/aim-notices/aim-notice-48.pdf*

ICGN Issues Viewpoint on Inclusions of Non-Voting or Limited Voting Shares in Stock Market Indices

On 5 December 2017, the International Corporate Governance Network (**ICGN**) issued a Viewpoint paper on the inclusion of non-voting or limited voting shares in stock market indices, following on from the ICGN Report of February 2017 on how differential ownership structures allow control over publicly listed companies that are disproportionate to the economic interests and cash flow rights of investors. ICGN Viewpoints provide opinion on emerging corporate governance issues and are intended to generate debate, while not defining a formal ICGN position on the subject.

In the Viewpoint, the ICGN set out its long-standing policy position that the optimal share structure for companies wishing to benefit from access to public capital should be one vote for each share within a same class. ICGN's general view is that mismatch of ownership and control through differential ownership rights can create significant governance risks for minority shareholders, such as management entrenchment and a lack of accountability. The Viewpoint explores whether or not non-voting or limited voting shares should be included in benchmark stock indices.

The Viewpoint can be found here:

- *https://www.icgn.org/sites/default/files/5.%20ICGN%20Viewpoint%20Indices%20and%20non%20voting%20shares.pdf*

QCA and UHY Hacker Young Publish Corporate Governance Behaviour Review 2017

On 5 December 2017, the Quoted Companies Alliance (**QCA**) published the QCA/UHY Hacker Young Corporate Governance Behaviour Review 2017. The review identifies how directors can improve their annual reporting to better connect with their shareholders.

The review's top five tips include:

- describe the relationship between your company's strategy and your governance arrangements effectively, and explain your board's role in realising the company objectives;
- articulate your company's story in an engaging way and take time to avoid boilerplate disclosures;
- set out clearly how your board's performance is evaluated and what is being done as a result;

- provide a single total remuneration figure for each of your directors within a focused remuneration report; and
- explain each director's role to demonstrate how your board has the appropriate balance of skills and experience.

The review can be accessed in full here:

- *http://www.theqca.com/article_assets/articledir_274/137401/UHY_QCA_Corporate_Governance_Behaviour_Review_report.pdf*

House of Commons Library Publishes Briefing Paper on Corporate Governance Reform

On 16 November 2017, the House of Commons Library published a Briefing Paper (Number CBP 8143) on Corporate Governance Reform. We discussed this in our October 2017 memorandum.

The Government announced nine reforms to corporate governance that it wants to bring into effect by June 2018, and this briefing discusses the Government's plans, related work in the area and other proposals.

The Briefing Paper can be accessed here:

- *http://researchbriefings.files.parliament.uk/documents/CBP-8143/CBP-8143.pdf*

Hampton-Alexander Review Publishes Supplementary Report on Improving Gender Balance in FTSE Leadership

On 9 November 2017, the Hampton-Alexander Review published a supplementary report assessing the progress made on gender balance in FTSE leadership. In its initial report, published a year ago, the Review set the following targets, in each case to be achieved by the end of 2020: for FTSE 350 companies, a minimum of 33% women's representation on their boards and, for FTSE 100 companies, a minimum of 33% women's representation on their leadership teams (either those who sit on a company's executive committee or those who directly report to members of that committee)

According to the report, women's representation on the boards of FTSE 100 companies stands at 27.7%, compared with 26.6% last year. However, if FTSE 100 companies are to hit the 33% target by the end of 2020, they will need to achieve the same rate of progress over the next three years as in the last three, with a step up in the appointment rate.

The report extends the FTSE 100 target to achieve 33% representation across leadership teams to FTSE 250 companies. The report states that, if the target is to be achieved by 2020, around 40% of all appointments will need to go to women over the next three years.

The report can be found here:

- *https://www.gov.uk/government/publications/ftse-women-leaders-hampton-alexander-review*

IA Publishes 2018 Principles of Remuneration

On 6 November 2017, the IA published an open letter to all FTSE 350 companies outlining key changes to The Investment Association Principles of Remuneration for 2018 (Principles).

The letter highlights changes in areas such as:

- Relocation benefits – these should now be disclosed at the time of appointment, be in place for a limited time and be fully detailed in the Remuneration Report; and
- Annual bonus – there is a requirement that bonus targets are disclosed within twelve months of the bonus payment, and that deferral is expected for any bonus opportunity greater than 100% of salary.

In addition, the letter emphasises certain aspects of the Principles to be considered for the 2018 AGM season, such as:

- Levels of remuneration – companies must adequately justify to investors the level of remuneration paid to executives, and take into account the wider social context of executive pay, rather than looking at benchmarking alone.
- Shareholder consultation – dialogue with shareholders on executive remuneration could be improved. Companies who withdraw resolutions prior to the AGM should ensure that they conduct a full analysis of shareholder feedback and consult further before re-submitting their Remuneration Policies.
- Pay for Performance – fund managers will be seeking greater transparency on both financial and non-financial bonus targets to ensure pay is in line with performance.
- Accountability of Remuneration Committee Chairs – investors are increasingly voting against the re-election of individual directors based on the decisions they make at the Remuneration Committee, and investors have a range of escalation approaches to voting policies here.

The press release containing links to the open letter and the principles can be found here:

- *https://www.theinvestmentassociation.org/media-centre/press-releases/2017/ia-publishes-pay-principles-for-ftse-companies-ahead-of-2018-agm-season.html*

ISS Announces 2018 Benchmark Voting Policy Consultation, Including Proposal on Virtual/Hybrid Meetings

On 26 October 2017, ISS, a leading provider of corporate governance and responsible investment solutions to the global financial community, announced the launch of its 2018 benchmark voting policy consultation. The ISS is seeking feedback on new policies or potential policy changes with respect to 13 voting policy areas. The area of most relevance to the United Kingdom is the proposal on the treatment of virtual/hybrid meetings. ISS suggests adding a new policy to the U.K./Ireland and European Voting Guidelines on virtual/hybrid shareholder meetings under which ISS will generally recommend proposals that allow for the convening of hybrid shareholder meetings and generally against those that allow for the convening of virtual-only shareholder meetings.

Comments will be taken into consideration as ISS finalizes the updates to its benchmark voting policies to be applied for shareholder meetings taking place on or after Feb 1, 2018. ISS expects to announce its final 2018 benchmark policy changes during the second half of November.

The closing date for feedback is 9 November 2017. The virtual/hybrid document can be found here:

- *https://www.issgovernance.com/file/policy/8-2017-comment-period-template-ukireland-and-europe-virtualhybrid-shareholder-meeting-proposals.pdf*

A press release with links to the various regional documents can be found here:

- *https://www.issgovernance.com/iss-launches-2018-iss-benchmark-policy-comment-period/*

Grant Thornton Publishes UK Corporate Governance Review 2017

On 17 October 2017, Grant Thornton published its U.K. Corporate Governance Review 2017. This provides a comprehensive analysis of the FTSE 350's annual reports. The review found that full compliance with all 55 provisions of the UKCGC is at 66%, the highest level ever. 95% of companies comply with all but one or two of the UKCGC provisions.

Topics covered include:

- risks and risk management
- culture reporting

- investor engagement; and
- board diversity

The review can be accessed here:

- *https://www.grantthornton.co.uk/globalassets/1.-member-firms/united-kingdom/pdf/publication/corporate-governance-review-2017.pdf*

UK FCA Issues First Fine for Non-Compliance With Derivatives Reporting Requirements

The FCA has fined Merrill Lynch International (**MLI**) over £34.5m for failing to report details of 68.5 million derivatives transactions in breach of EMIR and Principle 3 of the FCA's Principles for Businesses. This is the second largest FCA fine levied so far in 2017. This is the first ever enforcement action for failure to report details of derivatives transactions as required by EMIR. Under EMIR, since 12 February 2014, counterparties to derivatives contracts have been required to submit reports detailing those transactions to trade repositories. These reporting obligations seek to improve transparency in the derivatives markets.

Principle 3 of the FCA's Principles for Businesses requires firms to take reasonable care to organize and control their affairs responsibly and effectively, with adequate risk management systems. MLI breached this Principle because it failed to allocate sufficient personnel resources with the right level of EMIR reporting expertise to the reporting requirements, failed to conduct appropriate testing in relation to the reporting requirements and had an oversight system which did not review compliance with the reporting requirements in sufficient detail. As a result of these failures, an error with a static data table within MLI's reporting system which was causing the transactions to be unreported was not identified and corrected until February 2016.

In 2014, MLI had twice opened internal self-identified audit issues, identifying that it did not have governance and oversight in place to assess regulatory reports, and highlighting the Article 9 EMIR reporting requirement as a particularly high-risk area to be subject to review. No substantive steps were taken to address the risk until May 2015, when a pilot manual test was conducted. It was after manual testing was rolled out that the FCA raised questions with MLI over the detail of reports, resulting in MLI undertaking targeted testing through which it identified the error in the static data table.

As aggravating factors, the FCA took into account MLI's 2006 and 2015 reporting and transparency failings, and the fact that the FCA itself had directly communicated the importance of EMIR reporting requirements to firms in a number of ways. Mitigating factors were also identified. In particular, the FCA noted MLI's open and cooperative behaviour in self-reporting its breaches and quickly planning remedial work in relation to its systems and controls.

MLI received a 30% reduction in the overall fine because it agreed to settle at an early stage in proceedings. Had it not agreed to settle, the penalty would have stood at just over £49.3m.

- *View the FCA's Final Notice*.

US DEVELOPMENTS

SEC and NYSE/Nasdaq Developments

SEC Proposes Modernization and Simplification of Disclosure Rules

On 11 October 2017, the U.S. Securities and Exchange Commission (**SEC**) proposed certain amendments to Regulation S-K to simplify and streamline disclosures made by public companies and reduce compliance costs, while continuing to provide all material information to investors. The proposed amendments also seek to reduce duplicative and immaterial disclosure, leverage technology and improve the readability and navigability of disclosure documents. The amendments are part of the SEC's ongoing disclosure effectiveness review and implement a mandate under the Fixing America's Surface Transportation Act.

Highlighted below are some of the main proposed amendments:

- Management's Discussion and Analysis (**MD&A**) requirements:
  - *Year-Over-Year Comparisons in the MD&A*. *Elimination of the Earliest of the Three Years Included in the Financial Statements*. When financial statements included in a filing cover three years, a year-over-year discussion regarding the earliest year would not be required if (1) that discussion is not material to an understanding of the registrant's current financial condition, changes in financial condition and results of operations, and (2) the registrant has filed its prior year annual report on EDGAR containing MD&A of the earliest year.
  - *Elimination of the Reference to the Five-Year Selected Financial Data*. The SEC is proposing to eliminate the instruction to include trend related disclosure, where relevant, with respect to the five-year selected financial data, given trend disclosure is already required for liquidity, capital resources and results of operations. This proposal is intended to eliminate duplication and not intended to discourage providing trend disclosure.
  - *Flexibility in the use of presentations*. The proposed rules would allow companies to use any presentation that enhances a reader's understanding, thereby providing flexibility to choose the format deemed more appropriate to supplement or substitute the current year-over-year comparison that is ubiquitous in MD&A discussions.

Similar changes are also proposed for the "Operating and Financial Review and Prospects" section in Item 6 of Form 20-F, which would apply to annual reports filed by foreign private issuers.

- Omission of Confidential Information Without a Confidential Treatment Request: The proposed amendment would permit the omission of confidential information from material contracts without submitting a confidential treatment request to the SEC staff. When redacting a material contract exhibit, a company would still have to make a determination that information redacted from a contract was not material to investors and that its public disclosure would be competitively harmful to the company. The company, however, would not have to present its analysis to SEC staff when the redacted material contract is filed. Companies would be required to indicate with brackets where information has been omitted and include a prominent statement on the first page of the material contract. Please note that the SEC staff will, as part of its selective review of a company's filings, assess whether redactions from material contracts are limited to information that is not material and that would subject the registrant to competitive harm if publicly disclosed.

  The proposed amendment of this section would also apply to foreign private issuers who file on Form 20-F.

- Omitting Schedules and Exhibits from Exhibit Filings: This proposal would permit companies to omit entire schedules and similar attachments to filed exhibits unless the schedules or attachments contain material information that is not otherwise disclosed in the exhibit or the disclosure document. This would be similar to the existing accommodation in Item 601(b)(2) for plans of acquisition, reorganization, arrangement, liquidation or succession.

  This proposed amendment would also apply to foreign private issuers who file on Form 20-F.

- Expanded hyperlinking (Item 10(d)): While public companies are currently required to hyperlink to exhibits that are incorporated by reference from other filings, the proposed amendments include a proposal to expand hyperlinking by also requiring hyperlinks to information that is incorporated by reference in a periodic report or registration statement if that information is available on EDGAR. The intent is to improve readability and navigability of disclosure documents and discourage repetition.

  As discussed in our Q3 2017 Memorandum, the SEC recently adopted rules requiring hyperlinks to most exhibits filed pursuant to Form 20-F.

- Tagging cover page data: Under the proposed rules, all data points on the cover pages of Form 10-K, Form 10-Q, Form 8-K, Form 20-F and Form 40-F would be required to be provided in XBRL format (either inline or as an exhibit), and the number of data points companies are required to tag would be increased.

Comments on the proposed rule were due by 2 January 2018. The SEC's disclosure requirements will not change until the adoption of final rules by the SEC.

The SEC's proposed rule release is available at:

- *https://www.sec.gov/rules/proposed/2017/33-10425.pdf*

Our related client publication is available at:

- *http://www.shearman.com/en/newsinsights/publications/2017/10/sec-proposes-streamlining-disclosure-requirements*

US Treasury Department Issues Report on US Capital Markets

On 6 October 2017, the U.S. Department of the Treasury released a report on reforming the U.S. regulatory system for the capital markets (the "**Capital Markets Report**"). The Capital Markets Report includes 91 recommendations directed at financial regulators and Congress, many of which are targeted at the SEC.

Highlighted below are two of the main categories of recommendations addressed in the Capital Markets Report:

- Reducing Public Company Obligations:
  - For **public companies and companies considering an IPO**, the Capital Markets Report includes recommendations to: (a) repeal Dodd-Frank Act rulemaking mandates related to conflict minerals, resource extraction payments, mine safety and pay ratio disclosures, (b) reform the shareholder proposal process to make it harder for shareholders to submit proposals to be voted on at annual shareholder meetings and (c) review the role and regulation of proxy advisory firms.
  - The Capital Markets Report also recommends that the regulatory flexibility provided to newly public companies and smaller already reporting companies be extended, including by broadening the eligibility requirements for the scaled disclosure and reporting requirements applicable to smaller reporting companies from $75 million public float cap to a $250 million public float cap.
  - It also encourages the SEC to move forward on the various rule proposals and reports it has prepared related to its project to revise and reform its disclosure rules to make public company disclosures more effective. For additional information, please refer to "*SEC Proposes Modernization and Simplification of Disclosure Rules*" above.
  - Finally, it recommends that state governments and the SEC investigate ways to reduce the costs of securities litigation, including through the use of arbitration.

- Promoting Capital Formation:
    - A series of recommendations focuses on revising the recent SEC rules related to the crowdfunding and Regulation A+ private offering exemptions, including increasing caps on the amount of capital that can be raised.
    - Additionally, the Capital Markets Report recommends that the SEC review the definition of "accredited investor" with the goal of expanding the pool of eligible investors able to invest in private placements, as well as the ways in which private offering rules may unnecessarily restrict unaccredited investors from participating in private placements.

The Capital Markets Report is available at:

- *https://www.treasury.gov/press-center/press-releases/Documents/A-Financial-System-Capital-Markets-FINAL-FINAL.pdf*

Our related client publication is available at:

- *https://www.shearman.com/Perspectives/2017/10/Treasury-Issues-Report-and-Recommendations-on-Capital-Markets*

SEC Approves PCAOB New Auditor's Reporting Standard

On 23 October 2017, the SEC approved a new Public Company Accounting Oversight Board (**PCAOB**) auditor's reporting standard, which is aimed at offering investors more informative and well-grounded auditor's reports with more specific information about the audit undertaken.

The PCAOB new audit standard maintains the "pass/fail" opinion of the current auditor's report but includes the following changes:

- Critical Audit Matters (**CAMs**): The auditor has to expressly disclose the existence (or non-existence) of CAMs encountered in the audit, that is, any matter communicated or required to be communicated to the audit committee that relates to accounts or disclosures which are material to the financial statements, and that involves especially challenging, subjective or complex audit judgement.
- Other requirements: The audit report is required to disclose the years that the auditor has been in charge of the audit of the company, as well as to include a statement regarding the auditor's independence. The auditor's report has to be addressed to the shareholders and board of directors or equivalents of the company. Additionally, certain standardized language in the report has changed, and the auditor's opinion has been moved to the first section of the report. These requirements are intended to clarify the role of the auditor and its responsibilities.

All proposed new PCAOB rules, other than those related to CAMs, will be effective for the audits of fiscal years ending on or after 15 December 2017. On the other hand, the provisions related to CAMs will be effective as follows: (i) to audits for fiscal years ending on or after 30 June 2019 for large accelerated filers and (ii) to audits for fiscal years ending on or after 15 December 2020 for all other companies to which the requirements apply.

The PCAOB rules are available at:

- *https://www.sec.gov/rules/pcaob/2017/34-81916.pdf*

SEC Publishes New Guidance on Non-GAAP Financial Measures

On 17 October 2017, the staff of the SEC's Division of Corporation Finance updated its compliance and disclosure interpretations (**C&DIs**) regarding disclosure of non-GAAP financial measures in the context of business combination transactions.

The new C&DI states that financial measures included in forecasts provided to a financial advisor and used in connection with a business combination transaction are not considered non-GAAP financial measures if the following two conditions are met:

- the financial measures are included in forecasts provided to the financial advisor for the purpose of rendering an opinion that is materially related to the business combination transaction; and
- the forecasts are being disclosed in order to comply with Item 1015 of Regulation M-A or requirements under state or foreign law, including case law, regarding disclosure of the financial advisor's analyses or substantive work.

In disclosures of such financial measures in other circumstances, companies will be required to comply with the SEC's rules relating to non-GAAP measures, namely Item 10(e)(5) of Regulation S-K and Rule 101(a)(3) of Regulation G.

The SEC's C&DIs are available at:

- *https://www.sec.gov/divisions/corpfin/guidance/nongaapinterp.htm*

NYSE Prohibits Listed Companies From Issuing Material News Immediately After Market Close

On 7 December 2017, the NYSE announced a rule change, with immediate effect, pursuant to which NYSE listed companies are now prohibited from issuing material news after the close of the NYSE trading session (normally 4:00 p.m. ET) and until the earlier of: (i) five minutes after the official closing time for the NYSE trading session and (ii) the publication of the official closing price of the company's security.

This rule change will delay the timing of issuers' announcements delivered following market close, such as press releases announcing securities offerings. According to the NYSE, when a company releases material news after 4:00 p.m. but before the company's NYSE designated market maker has completed the closing auction, there can be significant differences between the official NYSE closing price and any price realised in another trading venue during such time window. The restriction does not apply to instances when companies release announcements to cure previous unintentional selective disclosure pursuant to Regulation FD.

The NYSE announcement is available at:

- *https://www.nyse.com/publicdocs/nyse/regulation/nyse/Material_News_Issued_Immediately_After_NYSE_Closing_Time_20171207.pdf*

House Passes Two Bipartisan Bills to Facilitate Securities Offerings

On 1 November 2017, the U.S. House of Representatives passed two bills designed to promote capital formation by (i) providing for extended JOBS Act testing-the-waters provisions to all companies, (ii) revising the definition of an "accredited investor" to allow a larger number of individuals to be eligible for participation in private placements and (iii) implementing the SEC's earlier expansion of confidential submission of draft registration statements by a non-emerging growth company (**non-EGC**) for its IPO and during the one-year period after going public. The bills have not reached the Senate floor yet. The bills would only become law if passed by the Senate and signed by the President.

In particular, *H.R. 3903*, the *Encouraging Public Offerings Act of 2017*, would expand certain JOBS Act provisions by allowing non-EGCs to undertake communications with institutional investors prior to the filing of a registration statement in order to measure investor interest and by providing for confidential submission of registration statements in connection with an IPO and during the one-year period after going public.

In addition, *H.R. 1585*, the *Fair Investment Opportunities for Professional Experts Act*, provides for an amended definition of "accredited investor" to include licensed or registered brokers and investment advisors and "any person determined by SEC regulation to have professional knowledge" related to a particular investment through education or job experience, as verified by FINRA or a similar self-regulatory organisation.

The bills are available at:

- *https://financialservices.house.gov/uploadedfiles/bills-115hr3903ih.pdf* (Encouraging Public Offerings Act of 2017);
- *https://www.congress.gov/115/bills/hr1585/BILLS-115hr1585rh.pdf* (Fair Investment Opportunities for Professional Experts Act)

SEC Updates Accounting and Financial Reporting Manual

On 1 December 2017, the SEC's Division of Corporation Finance released an updated version of its Accounting and Financial Reporting Manual.

The revisions relate to, among other things: (i) the pro forma impact of adopting new accounting standards; (ii) the consequences of adopting new accounting standards after status as EGC is lost; and (iii) clarifications on the effective dates for certain revenue standards for public business entities.

The updated SEC Manual is available at:

- *https://www.sec.gov/divisions/corpfin/cffinancialreportingmanual.pdf*

SEC Chairman Warns Investors of Risks Relating to Cryptocurrencies and Initial Coin Offerings (ICOs)

On 11 December 2017, SEC Chairman Jay Clayton released a statement on cryptocurrencies and ICOs as a warning to potential investors to beware of scams and criminal activity in the sector.

This statement was released following charges brought by the SEC against PlexCorps, a Bitcoin alternative which falsely promised huge profits to thousands of investors. This was the first action taken by the SEC's new Cyber Unit, which was created in September 2017 to focus the Enforcement Division's expertise on misconduct involving cyber-based threats. The SEC released a statement on 4 December 2017, announcing that PlexCorps would be the first in a series of crackdowns against cryptocurrencies.

Chairman Clayton offered his views on the topic, warning both main street investors and market professionals of the risks associated with cryptocurrencies and ICOs. He emphasised that, while cryptocurrencies change the manner of financial trading, they do not change the legal basis for regulation, noting that not a single initial coin offering has been registered with the SEC. Citing the "21(a) Report," an investigative report released by the SEC earlier this year, he highlighted that many professionals are attempting to claim that their tokens or coins are not securities. However, according to Chairman Clayton, cryptocurrencies do generally implicate the securities registration requirements and other investor protection provisions under the Securities Exchange Act of 1934. Therefore, prudence and caution are advised when making investments in this sector in order to ensure that proper regulation and protection laws are complied with.

The SEC's statement can be found online at:

- *https://www.sec.gov/news/public-statement/statement-clayton-2017-12-11*

Commission Staff Provides Regulatory Guidance for Accounting Impacts of the Tax Cuts and Jobs Act

On 22 December 2017, the President signed the Tax Cuts and Jobs Act into law, and, on the same day, the Staff announced publication of Staff Accounting Bulletin No. 118 (**SAB 118**) setting out its views about applying U.S. GAAP when preparing an initial accounting of the effects of the Tax Cuts and Jobs Act.

Under Financial Accounting Standards Board Accounting Standards Codification Topic 740, Income Taxes (**ASC 740**), regarding the reporting period that includes the enactment of the Tax Cuts and Jobs Act, the effects of changes in tax laws and rates must be recognised in the financial statements for the period in which such changes were enacted. Because the Tax Cuts and Jobs Act has only been enacted recently, there is a distinct possibility that the accounting for changes under the Tax Cuts and Jobs Act may be incomplete when the financial statements of a company will be issued. As such, SAB 118 provides for an extended "measurement period" in which companies facing this situation must comply with the following:

- where the calculations are complete: the effects of changes from the Tax Cuts and Jobs Act must be reported;
- where the calculations are not complete but reasonable estimates can be determined: the reasonable estimate would be reported as a "provisional amount" during the "measurement period"; and
- where the calculations are not complete and reasonable estimates cannot be determined: the inclusion of a provisional amount will not be necessary, and ASC 740 should continue to be applied based on the provisions of the tax law that were in effect immediately prior to the Tax Cuts and Jobs Act being enacted.

Such provisional amounts will need to be adjusted during a "measurement period" until the completion of the accounting under ASC 740, but may not extend beyond one year from the enactment date.

SAB 118 can be found at:

- *https://www.sec.gov/interps/account/staff-accounting-bulletin-118.htm*

Shearman & Sterling Publishes Recent Trends and Patterns in the Enforcement of the FCPA

On 2 January 2018, Shearman & Sterling published its bi-annual Trends & Patterns in FCPA Enforcement report (the "**FCPA Enforcement Report**"), which provides insightful analysis of recent enforcement trends and patterns in the United States, the United Kingdom and elsewhere, as well as helpful guidance on emerging best practices in FCPA and global anti-corruption compliance programs.

The FCPA Enforcement Report is an invaluable compendium of all FCPA-related developments in 2017, including U.S. foreign bribery proceedings and criminal prosecutions, DOJ foreign bribery civil actions, SEC actions, DOJ opinion releases, ongoing FCPA investigations, pre-FCPA prosecutions and parallel litigation related to the FCPA.

As is further detailed in the FCPA Enforcement Report, among the highlights from 2017 were:

- Thirteen corporate enforcement actions—six of which were announced prior to January 20—with total sanctions of approximately $1.95 billion, makes 2017 a significantly less active year in FCPA enforcement than 2016;
- Nearly half of the 2017 FCPA enforcement actions involved Latin America, while only one involved China—a sharp drop from the fifteen 2016 FCPA enforcement actions that involved China;
- The *Rolls-Royce* corporate and individual enforcement actions offer an interesting case study in the variety of jurisdictional hooks the Department of Justice has at its disposal, and how it often pushes the boundary of what should be permissible;

- The Supreme Court's decision in *Kokesh* has the potential to dramatically alter the way that the SEC brings FCPA enforcement actions, and comments from SEC officials suggest that the Commission has already begun to alter its approach in the wake of this decision; and
- One year into the Trump administration, it is clear that active enforcement of the FCPA will continue, albeit with some changes in the exercise of prosecutorial discretion at both the Department of Justice and the SEC.

The FCPA Enforcement Report is available at:

  - *https://www.shearman.com/perspectives/2018/01/shearman-recent-trends-and-patterns-in-fcpa*

SEC Provides an Update on the Implementation of the New Credit Losses Standard

On 4 December 2017, Robert B. Sledge of the SEC's Office of the Chief Accountant provided some remarks before the 2017 AICPA Conference on current SEC and PCAOB developments.

The two following points were addressed:

- General expected credit losses approach versus approaches for collateral dependent loans: The SEC recommends that, should foreclosure be likely to occur for collateral-dependent financial assets, a company should evaluate the expected losses by analysing such collateral's fair value. However, in the event that a company discovers that such asset is collateral-dependent, but foreclosure is not likely to occur, a practical expedient may be applied to measure expected credit losses based on the fair value of the collateral.
- Scope of PCI loans and PCD financial assets: Two pre-filing consultations were discussed to draw attention to the change from the purchased credit impaired (**PCI**) model to the purchased credit deteriorated (**PCD**) model under the new credit losses standard:
  - *Application of the PCI model by analogy*. A registrant acquired defaulted, discounted unsecured assets, and concluded that those transfers did not comply with the requirements of Topic 860 regarding the sale accounting. Consequently, he accounted for the transactions as the origination of new loans that are collateralized by the defaulted receivables. The Staff considered that Subtopics 310-10 and 310-20 "provided applicable and on-point guidance" for originated loans, and consequently such application of the PCI model by analogy was put into question.
  - *Application of the PCD model*. A registrant purchased consumer instalment loans immediately after they were originated by a retailer in connection with the sale of goods. These assets did not qualify for the PCD model according to the SEC, due to the fact that the credit-deterioration in connection with the purchased loans must be observed at the date of initial recognition.

The remarks of Mr. Sledge are available at:

- *https://www.sec.gov/news/speech/sledge-aicpa-2017-conference-sec-pcaob-developments*

SEC Releases Guidance on Certain Implications for Research Payment Arrangements Involving MiFID II Regulated Firms

On 26 October 2017, the SEC issued guidance to address certain extraterritorial issues under MiFID II, Europe's new financial regulation for investment business, which came into effect on 3 January 2018. One of MiFID II's aims is to give investors transparency into the cost of both research and trading commissions, by requiring payments for these elements to be unbundled.

In particular, the Staff of the SEC's Division of Corporation Finance (the "**Staff**") issued three no-action letters, designed to address concerns from U.S. broker-dealers and investment advisers regarding their need to charge for research in the manner required by their European clients under MiFID II. The Staff stated that they would grant relief under the following circumstances:

- The Staff would not recommend enforcement actions against an investment adviser that aggregates orders for the sale or purchase of securities on behalf of its clients in reliance on the position taken in the prior no-action letter for SMC Capital[1] while accommodating the differing arrangements regarding the payment for research that are required by MiFID II.
- The Staff will not recommend enforcement action if a broker-dealer provides research services that constitute "investment advice" under section 202(a)(11) of the Investment Advisers Act to an investment manager that is required to pay for the research services by using research payments under MiFID II. The relief is time-limited to 30 months from MiFID II's implementation on January 3, 2018.
- The Staff will not recommend enforcement action against a money manager seeking to operate in reliance on Section 28(e) of the Exchange Act if it pays for research through the use of a "Research Payment Account" and conforms to the requirements for "Research Payment Account" in MiFID II, provided that all other applicable conditions of Section 28(e) are met.

Our related client publication is available at:

- *http://www.shearman.com/en/newsinsights/publications/2017/11/mifid-ii-research-and-extraterritoriality-the-sec*

Noteworthy US Securities Litigation

Direct Evidence of Price Impact Not Always Required to Demonstrate Market Efficiency and Therefore Invoke Basic's Presumption of Reliance

On 6 November 2017, the Second Circuit Court of Appeals (which hears appeals from district courts in Connecticut, New York and Vermont) affirmed a class certification order in *Waggoner v. Barclays PLC*, a case concerning claims under the Securities Exchange Act of 1934 (the "**Exchange Act**") relating to the operation of alternative trading systems (so-called "dark pools"). The plaintiffs—three individuals who purchased American Depository Shares in Barclays PLC—had asserted claims against Barclays PLC, its U.S. subsidiary Barclays Capital Inc., and three senior officers of the companies for allegedly misleading the market by saying that Barclays monitored its alternative trading system (known as "LX") to protect clients from high-frequency traders.

The decision is significant for two reasons. First, it expands upon the Second Circuit's decision in *In re Petrobras Securities* to clarify that direct evidence of price impact is not always required to demonstrate market efficiency and thereby invoke the *Basic Inc. v. Levinson* ("***Basic***") presumption of reliance. Basic had established that plaintiffs may satisfy the reliance element of a claim under Rule 10b-5 without showing that they were actually aware of alleged misrepresentations if they met certain requirements, including demonstrating that the "stock at issue traded in an efficient market."

[1] SEC Staff stated that "the mere aggregation of orders for advisory clients, including collective investment vehicles in which the adviser, its principals or employees have an interest, would not violate [applicable laws] if the adviser implements procedures designed to prevent any account from being systematically disadvantaged by the aggregation of orders." (SEC No Action Letter, SMC Capital, 1995).

Second, the decision may be helpful to defendants in clarifying the limited applicability of the *Affiliated Ute Citizens of Utah v. United States* (“***Affiliated Ute***”) presumption where alleged omissions also relate to specific alleged misstatements. In *Affiliated Ute*, the Supreme Court explained that, in a case primarily involving a failure to disclose, positive proof of reliance is not required.

The district court granting class certification found that the predominance requirement for class certification—the requirement that questions of law or fact common to class members predominate over any questions affecting only individual members—was satisfied by the presumptions of reliance contained in both *Basic* and *Affiliated Ute*. The Second Circuit, however, found that the *Affiliated Ute* presumption of reliance does not apply where a plaintiff points to specific statements that are rendered misleading by material omissions, or even where the allegedly misleading nature of such statements is “exacerbated” by the omission. Rather, the *Affiliated Ute* presumption of reliance is appropriate only where “reliance as a practical matter is impossible to prove.” Because the plaintiffs had alleged numerous affirmative misstatements regarding Barclays’ LX system, and the omissions that were alleged directly related to specific alleged misstatements, the *Affiliated Ute* presumption did not apply.

The court affirmed class certification based on the Basic presumption of reliance, rejecting defendants’ argument that plaintiffs had not sufficiently demonstrated market efficiency because they had not shown that the price of Barclays’ securities reacted to new information. This holding expands on the court’s recent decision in *In re Petrobras Securities* (“***Petrobras***”) (which we discussed in our last newsletter and for which a petition for Supreme Court review has been filed), which noted that the burden of establishing market efficiency could be met through a combination of direct and indirect evidence, including direct evidence of price impact. Here, the court clarified that direct evidence of price impact is not required when other evidence of market efficiency is present.

Separately, the court rejected the defendants’ argument that the district court erred by imposing a burden of persuasion on the defendants to rebut the *Basic* presumption, rather than a mere burden of production (of evidence) that could permit a trier of fact to rule in the defendants’ favor. The Second Circuit reasoned that it would be inconsistent with *Halliburton Co. v. Erica P. John Fund, Inc*. (“***Halliburton II***”) to allow the defendants to rebut the *Basic* presumption by producing only limited evidence of market inefficiency. (In *Halliburton II*, the Supreme Court held that the defendants could rebut the *Basic* presumption by establishing that either (i) the alleged misrepresentation did not affect the market price, or (ii) the plaintiff would have bought or sold the security regardless.) Instead, the Second Circuit held that a defendant seeking to rebut the *Basic* presumption by demonstrating a lack of price impact must make that showing by a preponderance of the evidence.

Our related client publication is available at:

- *http://www.lit-sl.shearman.com/second-circuit-affirms-ldquodark-poolrdquo-class-*

Splitting With the Third Circuit, the Second Circuit Upholds Ruling Denying Noteholder’s Entitlement to a Make-Whole Premium

On 20 October 2017, the Second Circuit split with the Third Circuit Court of Appeals (which hears appeals from Delaware, New Jersey and Pennsylvania) regarding the entitlement of a noteholder to a “make-whole” premium in the case of a voluntary bankruptcy filing. A make-whole premium—often included in an indenture—is used to compensate noteholders for the loss of future interest payments in situations where the borrower voluntarily prepays its debt obligations.

Here, the Second Circuit held that noteholders were not entitled to payment of a "make-whole" premium following a voluntary bankruptcy filing. By contrast, the Third Circuit has held that certain noteholders are so entitled.

Between 2006 and 2012, MPM Silicones, LLC and its affiliates (collectively, "**Momentive**") incurred substantial debt obligations pursuant to various note indentures. One took the form of two classes of senior secured notes. The governing indentures called for the recovery of a make-whole premium if Momentive redeemed the notes prior to their maturity date, which was a fixed date stated in the indenture. The indentures also contained provisions for the automatic acceleration of the principal, premium, if any, and interest on the notes upon a default triggered by a bankruptcy filing. Although most events of default would give the senior lien noteholders the option of accelerating payment, the indentures provided that a default brought about by Momentive's voluntary bankruptcy petition would cause an automatic acceleration under the indentures.

In April 2014, Momentive filed for bankruptcy. Under its proposed plan of reorganization, Momentive issued replacement notes to the senior lien noteholders that did not account for the make-whole premium. Momentive sought a judicial determination that the noteholders were not entitled to payment of the make-whole premium. The bankruptcy court, siding with Momentive, confirmed the plan over the dissent of the noteholders and held, among other things, that the senior lien noteholders were not entitled to the make-whole premium because the indentures were not sufficiently explicit. The bankruptcy court further noted that the Second Circuit has made clear that a contractual automatic acceleration is not voluntary on the issuer's part. Finally, the bankruptcy court, relying in part on a Second Circuit case, *In re AMR Corp*. (**AMR**), concluded that the automatic stay of claims against the debtor's estate applied to de-acceleration of the senior lien notes, and that relief from the automatic stay was not warranted, because it would harm the debtors' estates by increasing the noteholders' claims by hundreds of millions of dollars.

The senior lien noteholders (among others) appealed, and the District Court for the Southern District of New York affirmed the decision. The Second Circuit affirmed the decisions of the lower courts as to the make-whole premium. The court rejected the senior noteholders' argument—that when *Momentive* issued the replacement notes under the Plan, it redeemed the notes prior to their maturity—for the same reason that argument was rejected in *AMR*. The bankruptcy filing triggered a default, which in turn automatically accelerated the debt, and that acceleration changed the maturity of the debt from a point in the future to the date of the bankruptcy filing. Therefore, the Second Circuit noted, even assuming that the issuance of replacement notes constituted a redemption, any subsequent redemption post-acceleration could not be considered voluntary or optional in nature; instead, the obligation to issue the replacement notes arose by operation of the automatic acceleration clauses in the indentures. A payment made mandatory by operation of an automatic acceleration clause, the court reasoned, is not one made at *Momentive's* option. The Second Circuit also held that the automatic stay barred the senior noteholders from rescinding the acceleration of the notes. The Second Circuit again cited *AMR* in concluding that a creditor's post-bankruptcy invocation of a contractual right to rescind an acceleration triggered automatically by a bankruptcy filing is barred because it would be an attempt to modify contractual rights, and therefore is subject to the automatic stay. As a result, the Second Circuit found that the make-whole premium was not owed to the senior lien noteholders.

The Second Circuit's decision creates a circuit split on the issue of entitlement to a make-whole premium under facts similar to those present here. The Third Circuit recently issued a decision that was critical of the decision at the bankruptcy court-level, and held that certain noteholders were entitled to payment of make-whole claims. Notably, the indentures at issue involved acceleration provisions similar to those in the indentures here. It will be up to the Supreme Court to resolve the split between the circuits (if it chooses to do so).

Our client publication is available at:

- http://www.shearman.com/en/newsinsights/publications/2017/11/entitlement-to-make-whole-payment-denied

Sixth Circuit Reverses Dismissal of Putative Securities Class Action, Finding Third-Party Complaints May Be Sufficiently "True" to Constitute New Information Under a Loss Causation Analysis

On 13 December 2017, the Sixth Circuit Court of Appeals (which covers appeals in Kentucky, Michigan, Ohio and Tennessee) reversed the dismissal of a consolidated putative class action against Community Health Systems, Inc. ("**Community**"), its CEO and CFO. The plaintiffs—shareholders of Community—alleged that Community and certain of its officers had violated Sections 10(b) and 20(a) of the Exchange Act by fraudulently inflating Community's share price through false and misleading statements regarding Community's operating model.

The holding—albeit limited to the Sixth Circuit— highlights that, when assessing the adequacy of loss causation allegations at the pleading stage, some courts may determine that information in the form of allegations in a related complaint may constitute true and new disclosures to the market.

The plaintiffs had alleged that the value of Community's shares fell immediately after a competitor, Tenet Healthcare Corporation, publicly disclosed in a civil complaint against Community expert analyses alleging that Community's profits depended largely on Medicare fraud, and fell further after one of Community's officers admitted to certain of Tenet's allegations. The district court, dismissing the putative class action complaint, found that, while the plaintiffs had sufficiently pled that the defendants intentionally made misleading statements, they had not adequately alleged that the misleading statements had caused the plaintiffs' losses because the disclosures came in the form of Tenet's complaint—and were therefore regarded by the market as mere "allegations" rather than truth. The Sixth Circuit reversed.

In considering loss causation, the court emphasized that the pleading requirement "is not meant to impose a great burden upon a plaintiff" but is rather "meant to prevent disappointed shareholders from filing suit merely because their shares have lost value and then using discovery to determine whether the loss was due to fraud." Thus, according to the Sixth Circuit, at the pleading stage a plaintiff need only provide a defendant with "some indication of the loss and the causal connection that the plaintiff has in mind."

Our client publication is available at:

- http://www.lit-sl.shearman.com/sixth-circuit-reverses-dismissal-of-putative-clas

Deputy Attorney General Rod Rosenstein Announces Revised FCPA Corporate Enforcement Policy

On 29 November 2017, Deputy Attorney General Rod Rosenstein announced a revised Foreign Corrupt Practices Act (**FCPA**) Corporate Enforcement Policy (the "**Policy**"), which represented a formalization, and extension, of the "FCPA Pilot Program" rolled out eighteen months earlier. The Policy cements the practice of rewarding companies that voluntarily disclose FCPA violations, fully cooperate with the government's investigation and remediate internal policies and conduct to prevent future wrongdoing. Mr. Rosenstein stated that he expects the Policy to "increase the volume of voluntary disclosures, and enhance [the Department of Justice's] ability to identify and punish culpable individuals." Acknowledging that the Department of Justice's (**DOJ**) internal policies do not create private rights and are not enforceable in court, Mr. Rosenstein reiterated that the program is intended to promote consistency by the DOJ's attorneys.

Mr. Rosenstein's remarks—and the recent history of corporate FCPA enforcement that he highlighted—are intended to provide additional motivation for corporations that uncover wrongdoing to disclose what they learn to the DOJ and remediate. Until more facts are known about the DOJ's approach across a broader range of cases, the effect of the Policy remains to be seen.

The full remarks are available at:

- *http://www.lit-wc.shearman.com/siteFiles/20039/Deputy%20Attorney%20General%20Rosenstein%20Delivers%20Remarks%20at%20the%2034th%20International%20Conference%20on%20the%20Foreign%20Corrupt%20Practice%20Act%20(November%2029,%202017).pdf*

Our client publication is available at:

- *http://www.lit-wc.shearman.com/deputy-attorney-general-rod-rosenstein-announces-*

Fourth Circuit Court of Appeals Affirms Dismissal of Securities Fraud Class Action, Stating that Scienter Cannot Be Pled by "Stacking Inference upon Inference."

On 15 November 2017, the Fourth Circuit Court of Appeals (which hears appeals from Maryland, North Carolina, South Carolina, Virginia and West Virginia) affirmed the dismissal of a putative securities fraud class action against PowerSecure International, Inc. ("**PowerSecure**"), and Sidney Hinton, its president and CEO. This case highlights the difficulty of pleading scienter (fraudulent intent) and further reinforces that, in order to do so, a plaintiff must plead facts that give rise to a strong inference that the defendants intentionally or recklessly deceived, manipulated or defrauded investors.

The plaintiffs alleged that the defendants defrauded investors by knowingly making misrepresentations about the renewal of a major contract in violation of Section 10(b) of the Exchange Act. The district court dismissed the complaint after finding that the plaintiffs failed to adequately allege scienter. The Fourth Circuit affirmed, stating that "[a] plaintiff may not stack inference upon inference" to satisfy the PSLRA's heightened pleading requirements for scienter.

In so doing, the court rejected the plaintiffs' primary argument that the defendants' alleged knowledge that the statement was false was sufficient to show scienter. The court explained that the plaintiffs' "argument fuses an inference that Hinton knew enough to realize that his characterization was technically incorrect with an inference that he intended it to deceive." "Stacking inference upon inference," the Fourth Circuit held, "violates [the PSLRA's] mandate that the strong inference of scienter be supported by facts, not other inferences."

The Fourth Circuit also found that the complaint, when taken as a whole, did not allow the court to draw a strong inference of scienter. First, the court found that the statement at issue did not support an inference that the defendants intended to deceive investors into thinking that PowerSecure could continue to serve the same region or otherwise maintain its profitability. Second, the court declined to find intent to deceive from the defendants' use of a "single *possibly ambiguous* word," noting that the fact of the contract's renewal "itself embraces the possibility that the new contract was not a renewal on identical terms." Finally, the court rejected the plaintiffs' attempt to establish scienter through Hinton's own sale and transfer of PowerSecure stock and observed that Hinton did not sell his shares when their value was at their peak and that the transfer of shares was made months after the alleged misstatement.

Our client publication is available at:

- *http://www.lit-sl.shearman.com/fourth-circuit-court-of-appeals-affirms-dismissal*

ITALIAN DEVELOPMENTS

Amendments to CONSOB Regulation on Issuers Implementing PRIIPs Regulation and Prospectus Regulation

On 28 December 2017, the Italian securities and exchange commission (*Commissione Nazionale per le Società e la Borsa*, "**CONSOB**") issued the resolution No. 20250 (the "**Resolution No. 20250**") amending CONSOB Regulation No. 11971 of May 14, 1999, as subsequently amended and supplemented (the "**Regulation on Issuers**"), and implementing (i) Regulation (EU) No. 1286/2014 on key information documents for packaged retail and insurance-based investment products (the "**PRIIPs Regulation**"), (ii) Commission Delegated Regulation (EU) No. 2017/653, supplementing the PRIIPs Regulation and (iii) Regulation (EU) No. 1129/2017 on prospectus to be published when securities are offered to the public or admitted to trading on a regulated market (the "**Regulation on Prospectus**"). The Resolution No. 20250 has entered into force effective from 1 January 2018.

In particular, pursuant to Article 4-*decies* of Legislative Decree No. 58 of February 24, 1998 (the "**Italian Consolidated Financial Act**"), documents containing key information (the "**KIDs**") for packaged retail and insurance-based investment products (the "**PRIIPs**") must be notified to CONSOB by the PRIIP manufacturer or by the PRIIP seller, as provided for by Article 10 of the PRIIPs Regulation. The purpose of KIDs is to facilitate the comprehension of PRIIPs and the comparison between different PRIIPs by retail investors.

In connection thereto, the newly introduced Article 34-bis.2 of the Regulation on Issuers establishes the procedure for the mandatory notification of KIDs to CONSOB, in accordance with the operational instructions published by CONSOB on 22 December 2017.

In addition, the Resolution No. 20250 also amends Article 57 of the Regulation on Issuers in order to align the cases of exemptions from the obligation to publish a prospectus set forth in Article 1, Paragraph 5 of the Regulation on Prospectus.

CONSOB and Borsa Italiana Regulatory Provisions Implementing MIFID II and MiFIR

On 29 December 2017, CONSOB issued the resolution No. 20249, replacing CONSOB Regulation No. 16191 of October 29, 2007, as subsequently amended and supplemented (the "**Market Regulation**"), in order to implement MiFID II and MiFIR. The new Market Regulation has entered into force effective from 3 January 2018.

In particular, the new Market Regulation redefines organizational and operational requirements for trading venues—such as regulated markets, multilateral trading facilities and the newly introduced organized trading facility—as well as transparency and reporting requirements for transactions in financial instruments, and establishes new limits for positions on commodity derivatives and data communication services.

In connection thereto, Borsa Italiana S.p.A., the managing company of the Italian stock exchange ("**Borsa Italiana**"), amended its Rules of the Market and the related Instructions in a two-step process.

In particular, on 20 November 2017, Borsa Italiana issued the notice No. 21822, effective from 27 November 2017, in order to introduce the first set of amendments concerning, *inter alia*, the termination of the regulated market SeDeX, the admission to trading on the new multilateral trading facility SeDeX, the categories of the markets participants and the market microstructure.

Finally, on 18 December 2017, Borsa Italiana issued the notice No. 23539, effective in part from 27 December 2017, in part from 2 January 2018, and in part from 3 January 2018, with the second set of amendments.

CONSOB Interim Update of Its Guidelines Concerning MAR

On 13 October 2017, CONSOB issued an interim update of its guidelines concerning (i) the management of inside information and (ii) investment recommendations (jointly, the "**Guidelines**"), in order to provide a handbook to issuers on the abovementioned matters, taking into account MAR and the relevant implementing measures, such as the guidelines and the Q&As issued by the ESMA.

In particular, the purpose of such interim update of the Guidelines is to include some of the observations collected during the relevant consultation period and to clarify the nature and therefore the strength of its provisions, whether compulsory or not (*i.e.*, soft law recommendations).

ASIA DEVELOPMENTS

SFC Issues Reminder on Cryptocurrency-Related Products and Derivatives

On 11 December 2017, the Securities and Futures Commission of Hong Kong (**SFC**) issued a circular, which reminds financial service providers of the legal and regulatory requirements associated with Bitcoin futures contracts ("**Bitcoin Futures**") and other cryptocurrency-related investment products. Furthermore, it cautions investors of the underlying investment risks, and investors should carefully weigh them against their own risk appetite.

Licensing and other regulatory requirements in Hong Kong

The circular notes that futures and commodities exchanges in the United States have launched or will soon launch Bitcoin Futures where Hong Kong investors may be able to trade through an intermediary, a member of these exchanges. Bitcoin Futures have the conventional features of a "*futures contract,*" which is defined in the Securities and Futures Ordinance (**SFO**) to include "*a contract or an option on a contract made under the rules or conventions of a futures market*." As such, Bitcoin Futures traded on overseas exchanges are subject to the rules of the respective exchanges and are regarded as "*futures contracts*" for the purposes of the SFO.

The circular sets out the following licensing requirements, which may apply to (i) any party who carries on a business in a "*regulated activity*" in Hong Kong; and (ii) any party who provides business services relating to Bitcoin Futures which constitute a "*regulated activity,*" irrespective of whether the party is located in Hong Kong, as long as it targets the Hong Kong public:

- carrying on a business in dealing in Bitcoin Futures, including those who relay or route Bitcoin Futures orders (Type 2 regulated activity – dealing in futures contracts);
- marketing a fund investing in Bitcoin Futures (Type 1 regulated activity – dealing in securities);
- managing a fund investing in Bitcoin Futures (Type 9 regulated activity – asset management); and
- providing advisory services in relation to Bitcoin Futures (Type 5 regulated activity – advising on futures contracts).

Intermediaries are also expected to strictly comply with the suitability requirement and other conduct requirements under the Code of Conduct for Persons Licensed by or Registered with the SFC when providing the above services.

The SFC also reminds the industry that other forms of cryptocurrency-related investment products, including cryptocurrency options, swaps and contracts for differences may, depending on their terms and features, be regarded as "*securities*" as defined under the SFO. Therefore, parties dealing in, advising on or managing such products in Hong Kong, or targeting such services to investors in Hong Kong, may be subject to the licensing, conduct and authorization requirements under the SFO.

Warning to investors

The circular highlights risks which investors may be exposed to in trading Bitcoin Futures and cryptocurrencies, including insufficient liquidity, high price volatility and potential market manipulation. The SFC warns investors that such risks may be magnified in trading Bitcoin Futures due to the speculative nature of the underlying assets and the leverage embedded in the products. Investors should be aware that, in some cases, the overseas exchanges may operate entirely outside of the SFC's jurisdiction, and some cryptocurrency exchanges have collapsed or been hacked in the past.

The circular is available at:

- *http://www.sfc.hk/edistributionWeb/gateway/EN/circular/doc?refNo=17EC79*

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