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GOVERNANCE & SECURITIES LAW FOCUS

Below is a summary of the main developments in U.S. and EU corporate governance and securities law and certain financial markets regulation developments since our last update on 19 January 2018.

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

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EU DEVELOPMENTS

Transparency Directive: ESMA Publishes Updated Guide to Notifications of Major Holdings

On 16 January 2018, the European Securities and Markets Authority (**ESMA**) published an updated version of its practical guide to the national rules across the EEA on the notification of major holdings under the Transparency Directive. The original version of the practical guide was covered in our April 2017 edition.

Part I of the practical guide provides a country-by-country summary of the main rules and practices regarding notifications of major holdings under the Transparency Directive. Part II presents key data across different jurisdictions in a table setting out notification thresholds, the triggering event, the deadline for learning of the triggering event and the deadline for making a notification.

The full text of the updated practical guide is available here:

- *https://www.esma.europa.eu/sites/default/files/library/practical_guide_major_holdings_notifications_under_transparency_directive.pdf*

European Commission Publishes Final Report on Sustainable Finance

On 31 January 2018, the European Commission ("**Commission**") published the final report by its High-Level Expert Group on Sustainable Finance (**HLEG**) ("**Final Report**"). On the same day, the Commission published a press release stating that it welcomes the Final Report.

The Commission established the HLEG to help develop an overarching and comprehensive EU strategy on sustainable finance. It requested advice regarding how to "steer the flow of capital towards sustainable investments; identify steps that financial institutions and supervisors should take to protect the financial system from sustainability risks; and deploy these policies on a pan-European scale."

The HLEG's Final Report presents various corporate governance recommendations in order to develop a sustainable financial system. The HLEG recommendations include:

- The extension of stewardship principles for institutional investors, for example by amending the Shareholder Rights Directive. Investors should have governance practices consistent with national requirements and the International Corporate Governance Network Global Stewardship Principles, ensuring in particular the alignment of their own incentives with long-term objectives and having sufficient expertise to address long-term sustainability risks.
- Investors should continuously engage with investee companies with the aim of preserving or enhancing long-term value on behalf of clients or beneficiaries. The extraction of short-term profits at the expense of long-term value creation should be avoided, and investors should integrate environmental, social and governance factors into stewardship activities.
- Investors with voting rights should seek in their voting process to make decisions addressing concerns over investee companies' sustainability performance.
- Requiring company management to develop a climate strategy and describe the company's approach to sustainable development goals.
- Ensuring that remuneration policies and individual executive employment contracts are consistent with the long term, including sustainability goals.

The full text of the Commission's report is available here:

- *https://ec.europa.eu/info/sites/info/files/180131-sustainable-finance-final-report_en.pdf*

The Commission's press release is available here:

- *http://europa.eu/rapid/press-release_IP-18-542_en.htm*

Commission Publishes Action Plan on Financing Sustainable Growth

On 8 March 2018, the Commission published an action plan on financing sustainable growth ("**Action Plan**"). The Action Plan builds on the recommendations set out in the Final Report published by the HLEG on 31 January 2018.

Regarding corporate governance, the Action Plan proposes to:

- Publish by Q2 2019 the conclusions of the fitness check on public reporting by companies launched by the Commission on 8 February 2018.
- Revise by Q2 2019 the guidelines on climate-related non-financial information (in line with the Financial Stability Board's Task Force on Climate-related Financial Disclosure), as well as utilise a new classification system for climate-related metrics.
- Request that the European Financial Reporting Advisory Group (**EFRAG**), where appropriate, assess the potential impact of new or revised IFRS standards on sustainable investments.
- By Q3 2018, establish a European Corporate Reporting Lab as part of EFRAG to promote innovation and develop the best practices in corporate reporting, including environmental accounting.
- Promote corporate governance that is more conducive to sustainable investments, by Q2 2019, by carrying out analytical and consultative work with relevant stakeholders. This will assess: (i) the possible need to require corporate boards to develop and disclose a sustainability strategy, including appropriate due diligence throughout the supply chain, and measurable sustainability targets; and (ii) the possible need to clarify the rules according to which directors are expected to act in the company's long-term interest.
- Collect evidence of undue short-term pressure from the capital markets on corporations and consider, if necessary, further steps based on this by Q1 2019.

The Action Plan states that the Commission will report on its implementation in 2019.

The full text of the Commission's Action Plan is available here:

- *http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52018DC0097*

The Commission's press release is available here:

- *http://europa.eu/rapid/press-release_IP-18-1404_en.htm*

Commission Publishes Evaluation and Fitness Check Roadmap on Public Reporting by Companies

On 8 February 2018, the Commission published for comment a roadmap detailing the proposed scope of its fitness check exercise, which will assess whether the public reporting obligations (both financial and non-financial) of EU companies with limited liability are meeting their objectives.

This fitness check will cover the Accounting Directive (including non-financial reporting), the Transparency Directive, and the Regulation on International Accounting Standards (**IAS**), among others. It will cover the various reporting requirements currently in force, taking into account the latest amendments of the Accounting Directive and the Transparency Directive in 2013, and the IAS evaluation in 2015.

In particular, the main issues on which the Commission seeks feedback are:

- Whether the current financial reporting framework meets its objective and will continue to do so.
- Whether the level of harmonisation and simplification meets the needs of all the various types of companies across the EU.
- Whether the disclosures in the area of environmental, social and governance reporting are fit for purpose.
- Whether the integration of different sets of public reporting will make the EU reporting framework more effective.
- Whether public corporate reporting takes enough consideration of digitalisation and technical progress.

Comments were invited by 8 March 2018 and the Commission intends to publish a staff working document ("**Staff Working Document**") in Q2 2019.

The full text of the evaluation and fitness check roadmap is available here:

- *https://ec.europa.eu/info/law/better-regulation/initiatives/ares-2018-744988_en*

Commission Launches Public Consultation on EU Framework on Public Reporting by Companies

On 21 March 2018, the Commission launched a public consultation aiming to take feedback from providers and users of financial and non-financial information regarding whether the EU framework on public reporting is still fit for purpose. This comes after the publication in February 2018 of the Commission's evaluation and fitness check roadmap on public reporting by companies, and is one of the actions announced as part of the Action Plan on financing sustainable growth published on 8 March 2018 that builds on the Commission's Final Report by its HLEG dated 31 January 2018.

The objectives of this consultation are:

- To assess whether the EU public reporting framework is, overall, still relevant for meeting its intended objectives, whether it adds value at the European level, is effective, internally consistent, coherent with other EU policies, efficient and not unnecessarily burdensome.
- To review specific aspects of the existing legislation as required by EU law.
- To assess whether the EU public reporting framework is fit for new challenges (such as sustainability and digitalisation).

The replies to this consultation will feed into the Staff Working Document that the Commission intends to publish on this subject in Q2 2019.

The consultation closing date is 21 July 2018.

Information regarding the Commission's consultation is available here:

- *https://ec.europa.eu/info/consultations/finance-2018-companies-public-reporting_en*

Commission Publishes Guidance on the 2018 Reform of Data Protection Rules

On 24 January 2018, the Commission published guidance on the reform of the EU data protection rules under the General Data Protection Regulation (**GDPR**), which will enter into application in May 2018. The guidance is contained in a communication to the European Parliament and Council titled "*Stronger protection, new opportunities - Commission guidance on the direct application of the General Data Protection Regulation as of 25 May 2018.*"

The new regulation provides for a single set of rules directly applicable in all member states, but it still requires significant adjustments in certain aspects, such as amending existing laws by EU governments and setting up the European Data Protection Board by data protection authorities. The guidance states the main innovations; the opportunities opened up by the new rules; takes stock of the preparatory work already undertaken; and outlines the work still ahead of the Commission, national data protection authorities and national administrations.

The guidance outlines the main elements of the new data protection rules:

- One set of rules across the continent.
- Same rules apply to all companies offering services in the EU.
- New and stronger rights for citizens.
- Stronger protection against data breaches.
- Stronger rules and deterrent fines.

The Commission requested in its press release regarding the guidance that member states speed up the adoption of national legislation in line with the GDPR, noting that only two member states so far had already adopted the relevant legislation.

The Commission has also identified a need to step up awareness of the benefits of the GDPR and compliance efforts with SMEs. Therefore, on the same day, the Commission launched a practical online tool to help SMEs and other organisations to comply and benefit from the new data protection rules.

The full text of the Commission communication regarding the guidance is available here:

- *http://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1517578296944&uri=CELEX%3A52018DC0043*

The background to the Commission guidance and related links are available here:

- *https://ec.europa.eu/commission/priorities/justice-and-fundamental-rights/data-protection/2018-reform-eu-data-protection-rules_en*

The Commission press release regarding the guidance is available here:

- *http://europa.eu/rapid/press-release_IP-18-386_en.htm*

The Commission's online tool for SMEs is available here:

- *http://ec.europa.eu/justice/smedataprotect/index_en.htm*

ESMA Publishes 2018 Regulatory Work Programme

On 1 February 2018, ESMA published its 2018 Regulatory Work Programme. The Regulatory Work Programme includes a list detailing the work to be done and consultations to be launched regarding various provisions of the Prospectus Regulation and the Market Abuse Regulation (**MAR**) in 2018.

The 2018 Regulatory Work Programme is available here:

- *https://www.esma.europa.eu/sites/default/files/library/esma20-95-823_2018_regulatory_work_programme.pdf*

ESMA Launches Stakeholder Survey

On 16 February 2018, ESMA launched a short stakeholder survey, seeking input from all market participants and other stakeholders on how they interact with ESMA. The survey asked questions such as what medium

stakeholders used to interact with ESMA, and how they rated the quality of ESMA's responses to their queries.

The survey was open for comments until 30 March 2018.

The survey and the explanation of the survey are available here:

- *https://www.esma.europa.eu/press-news/esma-news/esma-launches-stakeholder-survey*

A full overview of the ways ESMA currently interacts with its stakeholders can be found on the ESMA Website here:

- *https://www.esma.europa.eu/press-news/esma-news/esma-interacting-you-stakeholder*

ESMA Updates its Market Abuse Q&As

On 23 March 2018, ESMA updated its Questions and Answers (**Q&As**) on the MAR. The goal of the Q&A document is to promote common supervisory approaches in the application of the MAR and its implementing measures.

ESMA approved an update to the Q&As regarding Pillar 2 requirements and the obligation to disclose inside information. This is in order to fulfil the Minimum Requirement for own funds and Eligible Liabilities (**MREL**) exercise. MRELs should ensure that banks have enough capital and eligible liabilities to be bailed-in, where necessary, at all times. In the context of the MREL exercise (to be conducted by the Single Resolution Board in accordance with the Bank Recovery and Resolution Directive), whenever a credit institution subject to the MAR is made aware of information, it is expected to evaluate whether that information meets the criteria of inside information.

A main objective of the MAR is to enhance market integrity, and this is achieved through the prompt and fair disclosure of information to the public. Market abuse typically consists of insider dealing, unlawful disclosure of inside information and market manipulation.

The ESMA press release is available here:

- *https://www.esma.europa.eu/press-news/esma-news/esma-updates-its-market-abuse-qas*

The full text of the updated ESMA Market Abuse Q&A is available here:

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

ESMA Updates its Prospectuses Q&A in Relation to the Identification of Profit Forecasts

On 28 March 2018, ESMA published the 28th updated version of its prospectuses Q&A. There is a new Question 102 assisting in the understanding of the meaning of profit forecasts. This is the result of an analysis of the definition of "profit forecast" in the Prospectus Regulation. The main points that ESMA notes include:

- A profit forecast can refer to a range of figures, and need not refer to a precise figure.
- Profit forecasts are a different item to the trend information requirement in item 12 of Annex 1 of the Prospectus Regulation (809/2004). Forecasts should therefore be clearly identified. In the same manner, a stated aim does not necessarily amount to a profit forecast, particularly if a specific figure is mentioned. Equally, saying that a form of words is not a profit forecast does not stop a profit forecast from counting as one, if that is indeed what it amounts to.
- A profit forecast does not need to relate to the entirety of an issuer's results (for instance, it may refer to a segment of the issuer's business).

- "Likely level of profits or losses" does not necessarily refer just to the profit or loss for the year, but may refer to other measures of profitability. ESMA has adopted a "substance over form" approach.

The full text of the updated ESMA Prospectus Regulation Q&A is available here:

- *https://www.esma.europa.eu/file/23755/download?token=YSY1d4Rh*

The ESMA press release is available here:

- *https://www.esma.europa.eu/press-news/esma-news/esma-adds-new-qa-profit-forecasts*

UK DEVELOPMENTS

The London Stock Exchange Publishes Its Feedback on AIM Notice 49

On 8 March 2018, the London Stock Exchange published a feedback review for AIM Notice 49. It has confirmed that it will, subject to some minor changes, implement in full the amendments that it proposed to the AIM Rules for Companies and the AIM Rules for Nominated Advisers.

Some of the key implementations are:

- Formalising the "early notification process" (the requirement for nominated advisers of prospective AIM applicants to submit certain information about the applicant ahead of listing) in a manner similar to the current Schedule One form (which nominated advisers are familiar with).
- Permitting nominated advisers to state that insufficient information is available (where applicable) in certain situations in relation to the "early notification process."
- Creating a new obligation on AIM companies to disclose via their websites details of how they comply with (or, if they do not comply, explain their non-compliance with) existing, recognised corporate governance codes chosen by their respective boards of directors.
- Introducing new guidance for nominated advisers on the appropriateness of a new applicant to be admitted to trading on AIM.

The new versions of the rules came into force on 30 March 2018.

The full text of the feedback statement can be found at:

- *http://www.londonstockexchange.com/companies-and-advisors/aim/advisers/aim-notices/aim-notice-50.pdf*

The Pre-Emption Group Has Issued a Statement on Its Expectations for Disapplication Thresholds

As mentioned in our October 2017 edition, the Pre-Emption Group is committed to the pre-emption right thresholds outlined in its 2015 Statement of Principles. On 5 March 2018, it issued a statement to this effect in relation to the new Prospectus Regulation, which came into force on 20 July 2017.

A key focus of the statement is the exemption, which stems from the new Prospectus Regulation, from the obligation to publish a prospectus when issuing securities of the same class as those which are already admitted to trading which, over a period of 12 months, increase the total of those listed securities by less than 20%.

While the new Prospectus Regulation has increased the "admission to trading" prospectus exemption from below 10% to below 20%, The Pre-Emption Group has emphasised that it still supports the Pre-Emption Group Guidelines threshold for disapplication of pre-emption rights of no more than 5% (generally) and a further 5% for specified capital investment. The Pre-Emption Group also stated that it recognised that "decisions about

specific placings are a matter for individual shareholders" but then urged companies "to be mindful of the expectations included within the Statement of Principles."

In this statement, the Pre-Emption Group also encouraged companies to use its existing template resolutions when applying for authority to disapply pre-emption rights and issue shares.

The full text of this brief statement can be found at:

- *https://www.frc.org.uk/medialibraries/FRC/FRC-Document-Library/Preemption%20Group/050318-Pre-Emption-Group-)n-expections-for-disapplication-thresholds.pdf*

The Publication of Draft Companies (Disclosure of Address) (Amendment) Regulations 2018

The issue of directors' residential addresses being visible on Companies House has been a longstanding grievance for those directors concerned with their personal privacy. The Companies Act 2006 partially addressed this issue by allowing the filing of residential addresses for the purpose of public disclosure to be optional. However, directors and secretaries who had their addresses registered before the 1 January 2003 did not benefit from this ability to remove from the public record their residential addresses.

On 22 February 2018 the draft Companies (Disclosure of Address) (Amendment) Regulations 2018 were published with the aim of addressing this issue among a few others. These new draft regulations amend the Companies (Disclosure of Address) Regulations 2009 in several ways, the most salient among them being:

- Allowing individuals whose residential addresses are already on the register (under the pre- 1 January 2003 regime) to apply to Companies House to have the details of their residential addresses removed. This situation was only permitted under the 2009 Regulations if there was "a serious risk" that the individual, or a person living with them, would be subject to violence or intimidation as a result of the activities of a company with which they were involved.
- Where a company is required to maintain an address, allowing individuals to substitute the specified address for a service address provided by the applicant.
- Where individuals (as chargees) have been granted a charge in their favour by companies and such charge was registered before 1 January 2003, allowing applications for residential information on the register in this regard to be removed.
- In certain circumstances, allowing the registrar to remove all elements of an individual applicant's specified address apart from the outward code from the postcode, or any information in that address that shows a geographical area which is equivalent to or larger than the outward code of the postcode which applies to that address.

The Government has suggested that these regulations will come into force by the end of summer 2018.

The full text of the publication can be found:

- *http://www.legislation.gov.uk/ukdsi/2018/9780111165805/data.html*

The Government Responds to the Taylor Review of Modern Working Practices

On 7 February 2018, the Government published its response to "Good Work: the Taylor Review of Modern Working Practices." The Taylor Review of Modern Working Practices, published on 11 July 2017, considered in detail the implications of new types and forms of work on employee rights and employer responsibilities.

In the Government's response it alluded to the general increase of people in the U.K. working in "atypical forms," which has led it to reflect critically on key legal issues such as how to properly characterise employment statuses within the labour market.

The Government has made a number of commitments which will impact employers including:

- Extending the right to written particulars of employment to all workers (including those who may not technically qualify as employees) from day one of their "employment."
- Changing the law to improve pay transparency for agency workers and extending the right to an itemised payslip to all workers.
- Seeking to clarify what constitutes "working time" for those working in the "gig economy."
- Asking the Low Pay Commission to consider the potential impact of a higher national minimum wage/national living wage rate for non-contracted hours.
- Introducing a new "naming and shaming" scheme for employers who fail to pay the penalties issued to them by employment tribunals.
- Clarifying guidance on maternity pay and holiday allowance.
- The requirement to report certain information about the size and structure of a company's workforce. This will include (among other things) publicly disclosing models of employment, the use of agency services and reporting on how many requests have been received from zero hours contract workers to have fixed hours contracts.

Importantly, the response notes the Government's continued commitment to requiring companies to be specific about whether directors, in pursuing their duties, have taken account of wider matters. These matters include the interests of employees, and the fostering of relationships with suppliers as well as the maintenance of a reputation for high standards of business conduct.

The Government also expressed its commitment to working with the Financial Reporting Council in order to evaluate how guidance can be revised to encourage companies to provide better and more comprehensive explanations of their separate corporate practices. As part of this, the Government envisages that companies could be required to produce a "People Report" which would comprise a number of reporting requirements including gender pay gaps, diversity data and additional specific, employment related metrics.

The Government recognises that these commitments would impose "additional burdens" on businesses and also believes that an increase in reporting requirements should be implemented under existing and incoming legislation where possible.

The full text can be found at:

- *https://www.gov.uk/government/publications/government-response-to-the-taylor-review-of-modern-working-practices*

The FCA and the ICO Publish a Joint Statement on the GDPR for Financial Services Firms

On 8 February 2018, the Financial Conduct Authority (**FCA**) and the Information Commissioners Office (**ICO**) published a joint update on the EU General Data Protection Regulation (**GDPR**) in relation to financial services firms and their processing of personal data.

The FCA referred to the fact that the GDPR will apply in the U.K. (and across all member states) from 25 May 2018, and that in order to comply with some of the FCA's rules, financial services firms need to process "personal data" which will bring their activities within the ambit of the GDPR.

An outline is also provided on how "compliance with GDPR is now a board level responsibility" and reference is also made to the need for financial services firms to take steps to evidence to their compliance with the GDPR.

The GDPR will also impact on the future drafting of FCA rules itself, and so the joint statement also refers to potential changes to the requirements of certain sections of FCA rules. The need for firms to maintain and improve cyber resilience systems and controls and information technology generally was also stressed, which is unsurprising given the increased threat of cyber-attacks on financial services firms.

For the full text please see the official statement here:

- *https://www.fca.org.uk/news/statements/fca-and-ico-publish-joint-update-gdpr*

The ICGN Publishes Its Response to the FRC's Suggested Amendments to the UK CGC

On 23 February 2018, the International Corporate Governance Network (**ICGN**), a global investor-led body based in London with the general aim of promoting good governance in companies and responsible practices by investors, published its response to the Financial Reporting Council's (**FRC**) proposed revisions to the U.K. Corporate Governance Code (**U.K. CGC**). We discussed the FRC's consultation on its proposed revisions to the U.K. CGC in the January 2018 edition of this newsletter.

The ICGN response is split into a number of sections and addresses a range of important U.K. CGC issues such as "leadership and purpose," "division of responsibilities" and "remuneration."

Rather interestingly, the response comments on the need to look at institutional investor fiduciary duties from the perspective of the UN's "Sustainable Development Goals." The ICGN asserts that considering these "Sustainable Development Goals" may assist with sustainable value creation across companies and thus provide a benefit to end beneficiaries and investors alike.

In addition to addressing the topic of fiduciary duties, the ICGN response also addresses the absence within the U.K. CGC of any comprehensive discussion of the issue of "capital allocation." This, according to the ICGN, is an important topic as there have been instances of executives "inflating" their own pay via the use of share buyback procedures. This is an issue that the Government has already announced it will be further reviewing.

As such, a recommendation is made to the FRC to consider focusing more explicitly on this topic with the aim of drawing the attention of shareholders to the topic of capital allocation and thus enabling them to vote against buyback transactions which have the effect of facilitating "asymmetrical rewards" for company managers. This would supplement the ICGN's Global Stewardship Principles, which aim to provide a general frame of reference for institutional investors when performing their fiduciary obligations.

The full text of the ICGN's response can be accessed at:

- *https://www.icgn.org/sites/default/files/4.%20ICGN%20Comment%20FRC%20UK%20Corporate%20Governance%20Code%20Consultation%20Feb%202018_0.pdf*

The FRC has published all of the "non-confidential" responses it has received to its consultation on proposed revisions to the U.K. CGC. These can be accessed at:

- *https://www.frc.org.uk/consultation-list/2017/consulting-on-a-revised-uk-corporate-governance-co*

The OECD Publishes New Model Disclosure Rules for Common Reporting Standard Avoidance Schemes

In response to a request from the G7, the OECD published a press release on 9 March 2018 announcing the issuance of new Model Disclosure Rules. These new rules require professional advisors, banks and other service providers to disclose to tax authorities any schemes which have been put in place for their clientele in order to help them avoid reporting under the Organisation for Economic Co-operation and Development (the **OECD**)/G20 Common Reporting Standard regimes, or which obscure the true, beneficial identities of trusts and corporate entities.

The OECD also described how, following the implementation of the Common Reporting Standard on offshore financial accounts in over 100 jurisdictions this year, "€85 billion of additional tax revenue" has been collected. These new Model Disclosure Rules are aimed at ensuring greater disclosure of international tax avoidance schemes by shifting disclosure obligations onto "a wide range of intermediaries." The new rules also require that structures which conceal the beneficial owners of trusts, companies or offshore assets are reported to the relevant tax authorities.

Pascal Saint-Amans, a Director of the OECD Centre for Tax Policy and Administration, said in relation to the press release "the mandatory disclosure rules will be a powerful tool to detect taxpayers that continue to refuse to be compliant with their obligations to declare their assets and income to their tax authorities."

The full text of the press release can be read at:

- *http://www.oecd.org/tax/game-over-for-crs-avoidance-oecd-adopts-tax-disclosure-rules-for-advisors.htm*

A FAQ document was also published alongside the new rules and can be found at:

- *http://www.oecd.org/tax/exchange-of-tax-information/mandatory-disclosure-rules-questions-and-answers.pdf*

The Department for BEIS Publishes an 'Insolvency and Corporate Governance' Consultation Paper and the Pensions and the PLSA Publishes Its Response

On 20 March 2018, the Department for Business, Energy & Industrial Strategy (**BEIS**) published a consultation paper which proposes a number of measures aimed at improving corporate governance in companies which are in, or are approaching, insolvency.

The consultation also seeks suggestions from the public, as well as insolvency professionals and company directors, on other aspects of the wider corporate governance framework and whether these are working properly.

In particular, the consultation focuses on:

- The sales of businesses in distress, with recommendations being made to change aspects of regulation in order to ensure that directors who are responsible for the sale of an insolvent subsidiary take "proper account" of the interests of the subsidiary's stakeholders.
- Attempting to reverse situations where investors "rescue" companies in financial difficulties but then proceed to strip them of their assets ("value extraction schemes").
- Strengthening corporate governance in pre-insolvency situations by making recommendations on, among other things, how best to overcome issues arising from complex group structures, the payment of dividends, directors' duties and shareholder responsibilities.

The deadline for responding to the consultation is 11 June 2018.

The Pensions and Lifetime Savings Association's (**PLSA**) response to the consultation was published on 21 March 2018 and supports the need for attention to be drawn to best practice in insolvency situations following the high-profile issues surrounding the failures of BHS and Carillion.

In particular, the PLSA outlined the need for pension funds to play a "clear stewardship role" in order to ensure companies act in the best interests of their stakeholders thus ensuring that business activities have a "broader, positive impact on the economy and society."

The PLSA also stated that it would be working with its members and in close consultation with the BEIS in order to keep progressing the issue.

The full text of the consultation can be found at:

- *https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/691857/Condoc_-_Insolvency_and_Corporate_Governance_FINAL_.pdf*

The full text of the PLSA's press release regarding its response is available at:

- *https://www.plsa.co.uk/Press-Centre/Press-Releases/Article/PLSA-comments-on-BEIS-insolvency-and-corporate-governance-consultation*

BEIS Launches Inquiry on Executive Pay and Gender Pay Gaps in the Private Sector

On 23 March 2018, the House of Commons BEIS Committee announced that it has launched an inquiry into executive pay and the gender pay gap in the private sector.

Regarding gender pay gaps, the BEIS Committee has announced that it will look at how and whether businesses are complying with the relevant reporting requirements, whether the current regulations adequately cover staff salaries and what steps companies are taking to address the gender pay gap generally.

On the issue of executive pay, the BEIS Committee has said that it will look into whether any progress has been made in simplifying executive pay structures, whether remuneration committees are adequately reviewing executive pay and the extent to which "clawback provisions" have been used to recover cash and share bonuses in relation to examples of underperforming executives.

The BEIS Committee explicitly referenced the Equal Pay Act of 1970 and strongly condemned what it perceived as the lack of "fairness" which manifests itself in the gender pay gap and excessive executive pay.

Two evidence hearings are scheduled, one on gender pay reporting on 17 April and one on executive pay on 16 April.

The full text of the press release is available at:

- *https://www.parliament.uk/business/committees/committees-a-z/commons-select/business-energy-industrial-strategy/news-parliament-2017/corporate-governance-pay-launch-17-19/*

US DEVELOPMENTS

SEC and NYSE/Nasdaq Developments

SEC Adopts Interpretive Guidance on Cybersecurity Disclosures

On 21 February 2018, the Securities and Exchange Commission (**SEC**) released new interpretive guidance on public company disclosures regarding cybersecurity risks and incidents. The new interpretive guidance,

which reinforces and expands the guidance provided by the staff of the Division of Corporation Finance of the SEC on 13 October 2011, outlines the SEC's views regarding disclosures by public companies relating to cybersecurity risks, events and incidents under existing securities laws. It also outlines the SEC's views regarding the importance of appropriate disclosure controls and procedures, insider trading policies and selective disclosure safeguards in the context of cybersecurity incidents.

Although the interpretive guidance makes clear that the SEC views cybersecurity as a key disclosure matter, it does little to provide public companies with specific guidance on SEC expectations for what is required to be disclosed and when. The interpretive guidance does, however, present the following views of the SEC:

- Public companies should be describing the role that boards of directors have in cybersecurity-related risk management to the extent those risks are material to their businesses.
- Public companies should maintain adequate disclosure controls and procedures so that individuals responsible for disclosures are promptly alerted of cybersecurity incidents and a timely materiality and disclosure assessment can be made. Existing controls and procedures should be revisited to confirm their adequacy, and officers preparing certifications of periodic reports should consider the adequacy when providing such certifications.
- Public companies should have policies and procedures that restrict the ability of officers, directors and other insiders from trading before a decision has been made regarding the materiality and the disclosure necessary for a cyber incident.

The interpretive guidance does not provide any specific disclosure requirements that explicitly refer to cybersecurity matters. The guidance instead reiterates that the disclosure requirements related to cybersecurity risks and incidents are based on the relevant disclosure considerations that arise in connection with any business risk. It may be appropriate to provide disclosure regarding cybersecurity in the context of the following:

- risk factors;
- operating and financial review and prospects (**OFR**);
- description of the business;
- legal proceedings;
- financial statements; and
- disclosures of boards of directors' role in risk management.

Companies are not required to make disclosures that compromise their own cybersecurity efforts or those of law enforcement. However, companies must disclose cybersecurity risks and incidents that are material to investors in a timely manner. Companies may, in certain circumstances, be required to disclose such risks and incidents even before the completion of an internal investigation. In addition to making new disclosure, companies may have to amend or update prior disclosure.

In light of the guidance, companies should also consider the following:

- reviewing risk factor disclosures to ensure that the disclosures do not give the impression that the company has never been the target of, or subject to, a cybersecurity threat;
- disclosing any material ongoing cybersecurity spending, whether defensive or responsive to an actual incident, in the OFR; and

- engaging with the board regarding cybersecurity issues, specifically by reviewing with the board a summary of the interpretive guidance and reviewing the board's role in the oversight of cybersecurity matters.

While not expressly stating so, the interpretive guidance indicates that the SEC may be considering the following:

- new rules that specifically mandate the content and the timing of cybersecurity-related disclosures; and
- bringing the first enforcement cases against public companies related to inadequate cybersecurity disclosures or ineffective disclosure controls and procedures.

The SEC's interpretive guidance is available at:

- *https://www.sec.gov/rules/interp/2018/33-10459.pdf*

Our related client publication is available at:

- *https://www.shearman.com/perspectives/2018/02/sec-adopts-interpretive-guidance-on-cybersecurity-disclosures*

NYSE Introduces New Rules for Direct Listings

On 2 February 2018, the SEC approved the New York Stock Exchange's (**NYSE**) proposed rule amendments to facilitate non-IPO share offerings, or "direct listings," benefitting companies that wish to become public but do not need to raise capital.

A direct listing is an alternative to a traditional initial public offering (**IPO**). In a traditional IPO, the issuer engages one or more financial institutions to underwrite the offering and to assist the issuer in procuring purchasers for the shares and in pricing the offering. In a direct listing, however, shares are listed directly on an exchange without the involvement of underwriters.

Under the old rules, a company could directly list its shares on the NYSE only if the market value of the company's publicly held shares was at least $100 million based on an independent third-party valuation and the most recent trading price for the company's shares in a trading system for unregistered securities (the "**Private Placement Market**").

The amended rule eliminates the requirement that a company have common stock trading on a Private Placement Market. Instead, a company can now directly list on the NYSE if an independent third-party valuation determines that the market value of the company's publicly held shares is at least $250 million. The company must have an effective registration statement on file with the SEC and comply with other applicable NYSE listing requirements.

The new rules also:

- provide standards to determine whether the third party providing the valuation is independent;
- specify designated market-making requirements for directly listed shares in the event that the shares do not have a history of Private Placement Market trading;
- provide for a reference price for directly listed shares; and
- authorise the NYSE to declare a regulatory halt in securities that are the subject of an initial pricing on the NYSE and have been neither traded on an exchange or in an over-the-counter market immediately before pricing.

On 28 February 2018, Spotify Technology S.A. ("**Spotify**"), best known for its music streaming service, filed a Form F-1 in reliance on the new direct listing rules. Spotify has chosen to forego a traditional IPO despite the risks associated with a direct listing. These risks include an increased possibility of volatile early trading resulting from the lack of price discovery due to the fact that there are no underwriters to step in and stabilise the price. Spotify's direct listing will be a bellwether for whether direct listings can be a viable alternative to traditional IPOs.

The rule change is available at:

- *https://www.sec.gov/rules/sro/nyse/2018/34-82627.pdf*

The NYSE information memorandum describing the rule change is available at:

- *https://www.nyse.com/publicdocs/nyse/markets/nyse/rule-interpretations/2018/NYSE%20Info%20Memo%2018-02.pdf*

PCAOB and Accounting Firm Employees Charged With Misuse of Confidential Data to Improve Firm's Inspection Results

On 22 January 2018, the SEC announced civil charges against six certified public accountants for their role in an alleged scheme to misappropriate confidential information from the Public Company Accounting Oversight Board (**PCAOB**) relating to the PCAOB's planned inspections of an accounting firm, so that the firm could use the confidential information to help it avoid poor inspections.

On the same day, the United States Attorney's Office for the Southern District of New York announced the unsealing of an indictment charging five of the six defendants in the SEC action with conspiracy and wire fraud for their participation in the alleged scheme. The sixth SEC defendant had previously pleaded guilty (and had agreed to settle the SEC's claims) and is cooperating with the Government's investigation.

Three of the defendants are former PCAOB employees. These defendants shared confidential information from the PCAOB with the other three defendants, who were employees of the accounting firm. The defendants who worked for the accounting firm used the confidential inspection information to adjust the results of audits that were set for inspection by the PCAOB with a view to obtaining favourable inspection results.

Our related client publication is available at:

- *https://www.jdsupra.com/legalnews/pcaob-and-accounting-firm-employees-43258/*

SEC No-Action Letter Clarifies Securities Act Registration Exemption for Conversion to an SE

On 7 February 2018, the staff of the SEC's Division of Corporation Finance ("**Staff**") issued a no-action letter in connection with Constellium N.V.'s ("**Constellium**") proposed conversion to a European company (*Societas Europaea*, or **SE**). The no-action letter confirmed that the SEC would not recommend enforcement action if Constellium undertook the conversion without registration under the Securities Act of 1933 ("**Securities Act**"), in reliance on Securities Act Rule 145(a)(2).

Constellium's conversion to an SE comprised two steps:

- First, Constellium would convert from a Dutch public company with its registered office in the Netherlands, to an SE governed by the laws of the Netherlands with its registered office in the Netherlands, pursuant to the European Council Regulation No. 2157/2001 ("**Conversion**"). The Conversion would require shareholder approval.

- Second, Constellium would transfer its registered office from the Netherlands to France ("**Transfer**"). The Transfer, like the Conversion, would require shareholder approval.

Constellium acknowledged that both the Conversion and the Transfer trigger the registration requirements of the Securities Act. Under Securities Act Rule 145(a), an "offer, offer to sell, offer for sale, or sale" of securities occurs, thereby triggering the registration requirements, when "pursuant to statutory provisions of the jurisdiction under which [a] corporation . . . is organized, or pursuant to provisions contained in its certificate of incorporation or similar controlling instruments, or otherwise, there is submitted for the vote or consent of [the] security holders a plan or agreement for" a reclassification.

While Constellium intended to register the Transfer under the Securities Act, it sought no-action relief that the Conversion would not require Securities Act registration, on the basis that Securities Act Rule 145(a)(2) provides that registration is not required when "the sole purpose of the transaction is to change an issuer's domicile solely within the United States." Constellium pointed to a 2006 no-action letter, wherein the Staff found that the Rule 145(a)(2) exception applied when a German stock corporation organised under the laws of the Federal Republic of Germany converted to an SE.

The Staff agreed with Constellium's argument that the Conversion falls within the Rule 145(a)(2) exception and therefore does not require Securities Act registration. The Staff pointed to the following four facts in explaining its decision:

- after the Conversion, Constellium will remain a public limited company, and its registered office will remain in the Netherlands;
- the laws of the Netherlands will continue to apply to Constellium;
- the Conversion does not effect a change in national jurisdiction or a change of Constellium's registered office or seat from one EU Member State to another; and
- Constellium will register the Transfer on Form F-4.

The no-action letter is available at:

- *https://www.sec.gov/divisions/corpfin/cf-noaction/constelliumnv020718.htm*

Nasdaq Proposes to Modify Shareholder Approval Rule

On 30 January 2018, the Nasdaq Stock Market ("**Nasdaq**") filed notice with the SEC proposing to amend Rule 5635(d) regarding shareholder approval for certain securities issuances. The current Nasdaq shareholder approval requirements were adopted in 1990, and the rule generally requires shareholder approval when a listed company seeks to issue common stock equal to 20% or more of its outstanding common stock or voting power in a private placement (i.e., a transaction other than a public offering) at a price less than the greater of book or market value.

Nasdaq Rule 5005 currently defines "market value" as the closing bid price. Due to a number of complaints made by investors that this figure is not transparent and does not always reflect the actual price at which a security has traded, the proposed change would modify the measure of market value to the lower of "(i) the closing price (as reflected on Nasdaq.com) or (ii) the average closing price of the common stock (as reflected on Nasdaq.com) for the five trading days immediately preceding the signing of the binding agreement." Furthermore, the proposed change would delete the reference to "book value" in response to comments that book value is an accounting measure based on the historical costs of assets, as opposed to current value, and therefore not an appropriate measure of the dilutive effect of a potential transaction.

The text of the proposed rule change is available on the Nasdaq's website at:

- *http://nasdaq.cchwallstreet.com/NASDAQ/pdf/nasdaq-filings/2018/SR-NASDAQ-2018-008.pdf*

SEC Holds its Annual SEC Speaks Conference

On 23 and 24 February 2018, the SEC held its annual *SEC Speaks* conference in Washington, D.C. This year's conference was centred around the key themes of accessibility, flexibility and transparency. Senior SEC leadership provided remarks illustrating the SEC's 2017 accomplishments and priorities for 2018 and beyond.

Chairman Jay Clayton delivered opening remarks and reflected on his first year leading the SEC. He emphasised a need to focus on financial institutions as a means of protecting the long-term investments of "main street investors." This year's highlights also included remarks from Division of Enforcement officials, who discussed recent cases as well as priorities for 2018, which are largely concentrated around the areas of cybersecurity, cryptocurrency and retail investment. Robert Cohen, chief of the SEC's new Cyber Unit, described the unit's priorities as well as early success indicators.

New Commissioners Jackson and Peirce described their regulatory approach, with Commissioner Peirce placing a strong emphasis on economic analysis and Commissioner Jackson expressing the importance of melding law and finance together in order to prevent another financial crisis. The Divisions of Corporation Finance and Investment Management discussed the current issues on their radars, both placing an emphasis on cryptocurrencies and block chain technology. The Chief Accountant for the SEC, Wesley Bricker, reported on the effects of the Tax Cuts and Jobs Act of 2017. Acknowledging the uncertainty likely to be faced by companies with regard to their financial disclosures, he recommended a "triage" approach for reporting, by identifying (1) the effects that have taken place, (2) the effects that are likely to occur and (3) those that have been assessed but not yet quantified.

The speech transcripts are available at:

- *https://www.sec.gov/news/speeches*

Top Federal Securities and Commodities Regulators Testify on Virtual Currency Regulation Before Senate Banking Committee

On 6 February 2018, Chairman Jay Clayton of the SEC and Chairman J. Christopher Giancarlo of the Commodity Futures Trading Commission (**CFTC**), in their testimony before the U.S. Senate Committee on Banking, Housing and Urban Affairs, discussed the role of their respective agencies with respect to regulatory oversight of virtual currencies. In opening remarks and published testimonies, Chairman Clayton and Chairman Giancarlo emphasised their desire to ensure the safety and soundness of U.S. financial markets, as well as to punish those who engage in fraudulent, manipulative and deceptive conduct in the virtual currency marketplace.

Building on central themes from their recent joint op-ed published in *The Wall Street Journal*, Chairman Clayton and Chairman Giancarlo said that while they were confident that their agencies can achieve their regulatory mandates, they perceived potential gaps in the U.S. regulatory apparatus. For example, they said that the agencies lack authority to regulate some aspects of the virtual currency spot markets, often referred to as "exchanges." They said that these exchanges, which are generally subject only to state money transmission laws and CFTC anti-fraud and anti-manipulation regulations, require further consideration.

Chairman Clayton and Chairman Giancarlo said that they expect more virtual currency-related enforcement actions in the coming months. Chairman Clayton expressed frustration with the recent explosion of

unregistered initial coin offerings (**ICOs**), and those "gatekeepers" responsible for advising on such issuances—i.e., lawyers, investment bankers, accountants and consultants. He repeated his recent warnings to industry practitioners that "[t]okens and offerings that incorporate features and marketing efforts that emphasize the potential for profits based on the [...] efforts of others continue to contain the hallmarks of a security under US law."

Chairman Clayton said that the SEC is not yet ready to approve virtual currency-based exchange-traded funds or other funds available for retail investors, citing concerns about liquidity, valuation and custody of the funds' holdings and creation, redemption and arbitrage in the exchange-traded funds space.

Several Senators shared concerns over regulatory arbitrage in international virtual currency markets. Chairman Clayton and Chairman Giancarlo responded that while regulatory arbitrage is an open issue, they are optimistic that increased cooperation between U.S. regulators and within international bodies such as the Financial Stability Board and the International Organization of Securities Commissions will enhance stability in the global marketplace and assist regulators in achieving their respective aims.

Our related client publication is available at:

- *https://www.shearman.com/perspectives/2018/02/federal-securities-and-commodities-regulators-testimony*

GAO Report on SEC Efforts to Clarify Climate-Related Disclosure Requirements

Public companies have an obligation to disclose in their SEC filings material climate-related risks that could affect their finances and operations.

In this connection, in February 2018, the U.S. Government Accountability Office issued a report summarising a study carried out regarding (i) the steps taken by the SEC since 2010 to clarify the disclosure requirements for climate-related matters; (ii) the steps taken to examine the changes made by companies in their disclosure; and (iii) the constraints faced by the SEC in reviewing climate changes disclosures.

a. Steps to clarify disclosure requirements:

- In 2010, the SEC issued a guidance regarding disclosure related to climate change (*https://www.sec.gov/rules/interp/2010/33-9106.pdf*). Among other things, this guidance establishes four categories of climate-related risks (legislation and regulation, international accords, indirect consequences of regulation or business trends and physical impacts) and provides examples of how they could trigger disclosure requirements.
- Additionally, the SEC has been issuing comment letters on companies' climate-related disclosures.

b. Steps to examine changes in disclosures:

- In response to a request of the Senate Committee on Appropriations, the SEC issued two reports to Congress in 2012 and 2014 that examined changes to climate-related disclosure of 60 companies from six different industries. The reports concluded that there were no noticeable changes from year to year.
- In April 2016, the SEC requested feedback from stakeholders on the effectiveness of the disclosure requirements on topics such as climate change, resource scarcity, corporate social responsibility and good corporate citizenship. In December 2017, the SEC staff indicated they were considering the recommendations received.

c. Constraints faced: The SEC invariably faces certain constraints when reviewing the disclosures, mainly due to (i) companies' judgement on materiality of the information to be disclosed; and (ii) varying disclosure format among reporting companies.

The announcement and the report issued by the U.S. Government Accountability Office are available at:

- *https://www.gao.gov/assets/700/690196.pdf*
- *https://www.gao.gov/assets/700/690197.pdf*

Noteworthy US Securities Litigation

Second Circuit Vacates Class Certification Order and Reaffirms Standard for Defendants to Rebut 'Basic' Presumption of Reliance

On 12 January 2018, the Second Circuit Court of Appeals (which hears appeals from Connecticut, New York and Vermont) vacated a district court order certifying a securities fraud class action brought by purchasers of common stock in The Goldman Sachs Group, Inc. ("**Goldman**"). The district court had certified the class, ruling that defendants failed to rebut the presumption of reliance, as first articulated in *Basic Inc. v. Levinson* ("***Basic***"). According to the district court, the defendants did not "conclusively" prove a "complete absence of price impact," one of the requirements for rebutting the presumption—at the class certification stage—that the plaintiffs relied on the defendants' alleged misstatements.

On appeal, the Second Circuit ruled that, consistent with its precedent, defendants seeking to rebut the *Basic* presumption of reliance must do so by a preponderance of the evidence. Because it was unclear whether the district court applied a more demanding standard than preponderance of the evidence, the Second Circuit vacated the district court's decision and remanded it to consider the defendants' evidence under the proper standard.

In their complaint, the plaintiffs had alleged that Goldman and several directors made material misstatements about their efforts to avoid conflicts of interest in violation of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder. The plaintiffs claimed that the statements about efforts to avoid conflicts of interest were false and misleading because Goldman acted against the interests of its client in at least four collateralised debt obligations (**CDO**) transactions. The plaintiffs alleged that news of Government enforcement actions against Goldman related to the CDOs revealed the falsity of the defendants' statements and caused Goldman's share price to decline. Specifically, the plaintiffs claimed that, through these news reports, the market learned for the first time that Goldman had allegedly created "clear conflicts of interest with its own clients" by "intentionally packaging and selling securities that were designed to fail, while at the same time reaping billions for itself or its favoured client by taking massive short positions" in the same transactions.

In support of its motion for class certification, the plaintiffs argued that they met the "commonality" requirement for class certification, because common issues of law or fact predominated over issues affecting only individual members of the class. To establish 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—with respect to the element of reliance, plaintiffs argued that, under *Basic*, they were entitled to a presumption that all class members relied on the defendants' misstatements in choosing to buy Goldman's stock.

For their part, defendants attempted to rebut the *Basic* presumption by presenting evidence in the form of declarations and sworn affidavits that Goldman's stock experienced no price increase on the dates the alleged misstatements were made, and no price decrease on 34 occasions when the press reported Goldman's alleged conflicts of interest in the CDOs. The district court rejected the defendants' arguments and certified the class. In so holding, the district court ruled that the defendants failed to rebut

the *Basic* presumption because they "did not provide conclusive evidence that no link exists between the price decline [of Goldman's stock] and the misrepresentations."

In vacating the district court order and remanding for further consideration, the Second Circuit relied on its 2017 decision in *Waggoner v. Barclays PLC* (which we discussed in a previous memorandum), in which the court held that, in seeking to rebut the *Basic* presumption of reliance, defendants have the burden of persuasion and must rebut the presumption by a preponderance of the evidence. It ruled that the defendants failed to rebut the *Basic* presumption because they did not "conclusively" prove a "complete absence of price impact." Because it was unclear whether the district court required more of defendants than a preponderance of the evidence, the Second Circuit vacated the district court's order and remanded it for reconsideration.

Finally, the Second Circuit provided guidance to the district court on how to consider the defendants' evidence on remand. The Second Circuit noted that the district court had improperly construed the defendants' evidence as "an inappropriate truth on the market defense," or as evidence of the statements' lack of materiality, neither of which the district court thought it could consider at the class certification stage. The Second Circuit stated that the district court's view of the defendants' evidence was erroneous and that, on remand, the district court should evaluate the evidence to determine whether the defendants established by a preponderance of the evidence that the misrepresentations did not in fact affect the market price of Goldman' stock.

Resolving Circuit Split, Supreme Court Rules That Dodd-Frank Does Not Protect Internal Whistle-Blowers

On 21 February 2018, the United States Supreme Court unanimously held that the anti-retaliation provisions of the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act ("**Dodd-Frank Act**") only protect individuals who report violations of the securities laws to the SEC.

Writing for the Court in *Digital Realty Trust, Inc. v. Somers*, Supreme Court Justice Ruth Bader Ginsburg explained that the Dodd-Frank Act explicitly defined the term "whistle-blower" to include only individuals who report to the SEC and that, when a statute explicitly defines a term, courts must follow that definition. Therefore, she concluded, Paul Somers, who had reported only within his company, was ineligible for the whistle-blower protections under the Dodd-Frank Act.

Somers was employed by Digital Realty Trust for four years before he was fired in 2014, allegedly in retaliation for reporting to senior management that his supervisor had eliminated internal controls in violation of the Sarbanes-Oxley Act of 2002 (the "**Sarbanes-Oxley Act**"). Somers did not report those violations to the SEC, and he did not rely upon the Sarbanes-Oxley Act's own remedial scheme for retaliation against whistle-blowers. Instead, Somers sued Digital Realty Trust in federal court in California under the Dodd-Frank Act whistle-blower anti-retaliation provisions.

That court denied Digital Realty Trust's motion to dismiss, in reliance on an SEC rule, promulgated under the Dodd-Frank Act, that defined the term whistle-blower, for purposes of the Dodd-Frank Act's anti-retaliation protections, to include individuals who reported only internally. The Ninth Circuit Court of Appeals (which hears appeals from Alaska, Arizona, California, Hawaii, Idaho, Montana, Nevada, Oregon, Washington and the territories of Guam and the Northern Mariana Islands) affirmed. It reasoned that applying the more limited statutory definition would narrow the protection "to the point of absurdity," and therefore that the Dodd-Frank Act's anti-retaliation provisions must include individuals who report only internally, without reporting to the SEC. Previously, the Fifth Circuit Court of Appeals (which hears appeals from Louisiana, Mississippi and Texas), when faced with this question, held that "employees must provide information to the SEC to avail

themselves of Dodd Frank's anti-retaliation safeguard," but the Second Circuit reached the same conclusion as the Ninth Circuit.

In resolving the circuit split, the Supreme Court reversed the Ninth Circuit and concluded that the SEC's rule interpreting the term "whistle-blower" did not merit deference in light of the plain language of the Dodd-Frank Act. The Court found no ambiguity in the statutory definition of "whistle-blower," which expressly included only individuals who reported to the SEC. This interpretation, the Court reasoned, was supported by the underlying purpose of the Dodd-Frank Act: "to motivate people who know of securities law violations to tell the SEC."

The Court disagreed with the Ninth Circuit that applying the narrow definition would reduce protection "to the point of absurdity," on the grounds that the Dodd-Frank Act still "protects a whistle-blower who reports misconduct both to the SEC and to another entity, but suffers retaliation because of the latter, non-SEC, disclosure." The Dodd-Frank Act thus protects whistle-blowers if they disclose alleged violations to the SEC, even if a contemporaneous disclosure to a company itself is the true cause of any retaliation.

The decision could have negative consequences for corporations covered by the whistle-blower rules. If their employees, with the benefit of counsel, conclude that they have greater protection against retaliation if they report misconduct to the SEC, the ruling could end up discouraging internal reporting and encouraging whistle-blowers to circumvent any internal hotlines that the company has established.

Record-Breaking Whistle-Blower Awards Continue Incentives to Report Misconduct to the SEC

On 19 March 2018, the SEC announced three multi-million dollar awards to whistle-blowers to reward them for reporting misconduct. One whistle-blower received $33 million, which constitutes the largest SEC whistle-blower award in history; the two other whistle-blowers will split a $50 million award. These significant awards continue a trend of rising awards by the SEC, which continues to focus on publicly incentivising and protecting whistle-blowers.

In response to the recent record-breaking awards, Jan Norberg, Chief of the SEC's Office of the Whistle-blower, commented that, "We hope that these awards encourage others with specific, high-quality information regarding securities laws violations to step forward and report it to the SEC." Indeed, since 2012, the SEC has awarded over $262 million to 53 whistle-blowers, with an average award of approximately $5 million.

The SEC's promise of substantial awards for whistle-blowers is bolstered by its active pursuit of enforcement actions against companies that retaliate against whistle-blowers or take steps that can be construed as impeding reporting in violation of the Dodd-Frank Act and the Sarbanes-Oxley Act. Since 2014, the SEC has brought enforcement actions against two companies for alleged retaliation against whistle-blowers, eight for allegedly impeding whistle-blowers from reporting misconduct, and one for both, resulting in a total of $19 million in penalties. While some of these fines have been modest considering the size of the corporations that paid them, these cases also expose the companies involved to private litigation brought by the whistle-blowers themselves, which can significantly increase the financial risk. For example, in 2017 a jury found that Bio-Rad violated the Sarbanes-Oxley Act and Dodd-Frank Act whistle-blower provisions when it fired its general counsel, who had reported suspected violations of the Foreign Corrupt Practices Act to the company's audit committee. The general counsel was subsequently awarded over $8 million in lost wages and punitive damages, as well as $3.5 million in litigation costs by the court.

The potential for a multi-million dollar award and the option to sue for damages and penalties if subjected to retaliation combine to create a strong incentive for potential whistle-blowers to report to the SEC. And every headline-grabbing award prompts even more potential whistle-blowers to take notice.

Supreme Court Holds That State Courts May Hear Securities Class Actions

On 20 March 2018, the United States Supreme Court, in a unanimous decision, ruled that state courts have jurisdiction to adjudicate class actions brought under the Securities Act and that such actions cannot be removed from state to federal court.

By way of background, the Securities Act authorised both federal and state courts to exercise jurisdiction over private causes of action relating to securities offerings and barred removal of such suits from state to federal court. In 1995, in order to stem perceived abuses of the class-action mechanism in securities litigation, the U.S. Congress enacted the Private Securities Litigation Reform Act (**PSLRA**). The PSLRA amended the Securities Act by introducing procedural reforms for securities class actions in federal court. When plaintiffs began filing securities class actions in state courts instead, to avoid the federal procedural standards, Congress passed the Securities Litigation Uniform Standards Act of 1998 (**SLUSA**).

Cyan, Inc. ("**Cyan**"), a telecommunications company, and its officers and directors argued that the SLUSA amendments gave federal courts exclusive jurisdiction over class actions brought under the Securities Act. The Supreme Court disagreed, and held that those amendments did not divest state courts of concurrent jurisdiction over class actions pursuant to the Securities Act. The Court, rejecting a separate argument regarding removal of such actions, held that SLUSA does not permit defendants to remove class actions alleging only Securities Act claims from state to federal court.

This decision may result in more Securities Act class actions being brought by plaintiffs in state courts across the country, including those located in districts that previously had held that SLUSA deprived state courts of jurisdiction over such actions. Several other points are worth noting:

- *First*, as the Supreme Court emphasised, the PSLRA "included substantive sections protecting defendants (like a safe harbour for forward-looking statements) in suits brought under the federal securities laws" and, "wherever those suits go forward, the [PSLRA]'s substantive protections necessarily apply." The Court did not address whether some of the most important PSLRA protections—such as the discovery stay pending a motion to dismiss—are "substantive" or "procedural." Moreover, the case does not undermine a defendant's ability to seek to stay *discovery* in a parallel state action while a motion to dismiss is pending in federal court, coordinate multiple parallel actions, or stay one action entirely while another proceeds.
- *Second*, other potential avenues for removal of Securities Act claims are unaffected. The Court's opinion addressed only removal under SLUSA, not removal on other grounds. For example, "related to bankruptcy" removal—a critical route to federal court for underwriters, directors and officers, and audit firms in cases where the corporate issuer has filed for bankruptcy, alleged damages may be large and the ability to collect on indemnification rights may be affected—is untouched by the Court's decision.
- *Third*, the case may lead more companies to consider adopting bylaws that designate federal courts as the exclusive forum for resolution of claims under the Securities Act. Such bylaws are currently being challenged in litigation pending in Delaware Chancery Court, which is receiving close attention in the securities bar.
- *Finally*, as the Court noted, a legislative solution is available. Ending state court jurisdiction over Securities Act class actions, or at least permitting removal, would arguably give greater coherence to the statutory scheme. Class actions under both the Exchange Act of 1933 and state law are already channelled to federal court, so class actions filed exclusively under the federal Securities Act are in that respect an outlier.

ITALIAN DEVELOPMENTS

CONSOB Approves the New Intermediaries Regulation

On 15 February 2018, the Italian securities and exchange commission (Commissione Nazionale per le Società e la Borsa, "**CONSOB**") issued resolution No. 20307, approving the new regulation on intermediaries (the "**Intermediaries Regulation**").

This concludes the phase of implementation in Italy of MiFID II and MiFIR, reinforcing safeguards for investors on financial instruments distributed by intermediaries and/or traded on trading venues in the European Union. The new Intermediaries Regulation was drawn up on the basis of the results of the consultations with the market started in the second half of 2017.

The Intermediaries Regulation contains in particular:

- the provisions for the protection of investors, including the requirements of knowledge and competence for the personnel working in intermediaries who provide information or advice to clients;
- the new regulation of the activity of financial advisors and, implementing the provisions of the 2016 Stability Law, of the new supervisory and sanctioning powers of the supervisory board and the single register of financial advisors; and
- the authorisation procedures of investment firms, the access of the EU and extra-EU investment companies into the Italian market and the MiFID II implementing regulations applicable to the managers.

CONSOB Approves the Regulation Concerning Reporting Information of a Non-Financial Nature

On 18 January 2018, CONSOB issued resolution No. 20267, approving the regulation on reporting obligations concerning information of non-financial nature, thus implementing legislative decree No. 254 of December 30, 2016.

Starting from financial year 2017, listed companies, banks and insurance companies satisfying certain requirements (i.e., certain financial parameters; more than 500 employees) are required to file with CONSOB and disclose to the market a report on information of a non-financial nature, relating to environmental and labour profiles, respect for human rights and the fight against corruption.

Such reports, audited by independent auditing companies, allow investors to easily access non-financial information concerning specific companies.

Borsa Italiana Approves a New Version of its Rules of the Market and Related Instructions for Fine Tuning Amendments Concerning Privileged Information Disclosure in IPO Process

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 (new versions will enter in force as of May 2018).

In particular, Borsa Italiana decided to postpone disclosure obligations under MAR during IPO processes on MTA, MIV and MOT markets, distinguishing two different phases: the admission to listing phase and the admission to trading phase. Given that under the new rules the first phase is a due diligence phase aimed at assessing the company's eligibility to the listing, while the second phase is focused on the technical evaluations of the financial instruments to be admitted to trading, the disclosure obligations under MAR are postponed to the second phase. The new rules are aligned with the disclosure obligations applicable in the rest of the EU.

Amendments to the Italian Consolidated Financial Act Concerning European Long-Term Investment Funds

As of 15 February 2018, an amended version of Legislative Decree No. 58 of February 24, 1998 ("**Italian Consolidated Financial Act**") entered into force, in order to implement the provisions of the EU Regulation No. 760 of 2015, on European long-term investment funds.

Such amendments outline the scope of action for CONSOB, which still must provide its implementing regulation on the matter.

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