

Capital Markets Group Legal Alert

Disclosure and Model Code obligations in respect of the use of shareholdings as security

The FSA has recently received a number of queries regarding the disclosure obligations of persons discharging managerial responsibilities (“PDMRs”) as a result of the FSA’s investigation of the entrepreneur David Ross in December. Mr Ross belatedly disclosed that he had pledged shares in four companies of which he was a director as security against his personal loans. In order to clarify the position, the FSA released a statement on Friday 9 January 2009 setting out the disclosure requirements for PDMRs who grant security over their shareholdings. The FSA has confirmed that such grants of security over shares (by the creation of a security interest such as a mortgage, charge, or pledge), are covered by the disclosure requirements in the Disclosure and Transparency Rules (“DTR”).

The rule in question is DTR 3.1.2R, which sets out that PDMRs (defined as the directors of the issuer, or senior executives of the issuer who are not directors but who have regular access to inside information or have power to make managerial decisions affecting the future development and business prospects of the issuer), and their connected persons must notify the issuer in writing of the occurrence of all transactions conducted on their own account in the shares of the issuer, or derivatives or any other financial instruments relating to those shares, *within four business days of the day on which the transaction occurred*. Directors and their connected persons should therefore disclose grants of security over shares to the company of which they are a director which, in turn, should make disclosure to the market. The definition of a PDMR in DTR 3 only applies to directors of an issuer registered in the United Kingdom that has requested or approved admission of its shares to trading on a regulated market, and

therefore does not apply to AIM companies. It is however likely that AIM companies would need to disclose the use of shareholdings as security under Rule 17 of the AIM Rules, although this was not addressed in the FSA guidance. Directors of AIM companies should therefore discuss with their Nomads whether disclosure of specific security interests should be made.

The DTRs are derived from the EU Market Abuse Directive. They do not provide any general guidance on what transactions will be considered to be conducted “on a person’s own account”. This has led to differing approaches in some Member States, and has caused uncertainty amongst London practitioners regarding the scope of the disclosure obligations in respect of the use of shareholdings as security. The FSA recognises this ambiguity, and as a result has concluded that it will not pursue any enforcement action against directors who have not made the necessary DTR disclosures to date. However, PDMRs who have granted security over shares should now disclose this to the market *as soon as possible, and all outstanding disclosures should be made by 23 January 2009*. This applies irrespective of the date on which the security interest was created, and prompt disclosure should therefore now be made even if the creation of the security interest pre-dated the DTR coming into force.

In addition, the FSA has stressed that the Model Code requires listed issuers and their PDMRs to obtain clearance for any share “dealings”, which include “using as security, or otherwise granting a charge, lien or other encumbrance over the securities of the company”. The FSA has emphasised that a director should obtain clearance where his or her shares are to be used as collateral for a financing transaction, and that listed issuers should deal with Model Code breaches by their directors. However, there is no obligation under the Model Code for the director or the company to disclose such dealing to the market.

If you have any questions or require specific advice on any matter discussed in this publication, please contact Stephanie Bates, William Charnley, Angela Hayes, Justine Usher or your regular contact at Mayer Brown.

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