

Pre-Emption Group

Monitoring Report

May 2017



Contents	<i>Page</i>
Introduction	1
Monitoring of market practice	3
FTSE 350	
FTSE Small Cap	
FTSE Fledgling	
Issuances in other indices or listings	
Level of Support for Disapplication Authorities	
Conclusion.....	11
Appendix of best practice in engagement and disclosure.....	12
Contacting the Pre-Emption Group	14

Introduction

1. Pre-emption approval is an important element of investor protection in UK company law, giving existing shareholders the right to subscribe for their pro rata portion of any new shares issued for cash. These rights may be disapplied only by a special resolution of shareholders at a general meeting of the company.
2. In addition to the statutory pre-emption provisions, any company with a premium UK listing which is incorporated outside the UK is required to ensure that its constitution provides for rights of pre-emption for shareholders that are at least equivalent to those that apply to UK incorporated companies.
3. In 2015, after a six year break since the last consideration of the Statement of Principles, the Pre-Emption Group (PEG) was re-formed under the Chairmanship of Mr Robert Swannell. The PEG considered market changes, developments in best practice and whether consequential revisions were appropriate and issued a revised Statement of Principles in March 2015. Whilst the Statement of Principles is not a rulebook it aims to provide clarity on the factors to be taken into account when considering the case for disapplying pre-emption rights and making use of an agreed authority for a non-pre-emptive share issue and the circumstances in which flexibility might be appropriate. Companies and investors are encouraged to use the Statement of Principles as a basis for discussion of the business case as they consider pre-emption issues.
4. When the revised Statement of Principles was published, the PEG undertook to issue monitoring reports on its application. The first monitoring report was published last year and after considering the results, as well as investors' views on best practice, the PEG decided to assist companies by publishing template resolutions for authorities to disapply pre-emption rights. The template provides for companies to propose two resolutions for the two separate five per cent disapplication authorities. The resolution to disapply pre-emption rights in relation to an additional five per cent specifically references use only in connection with an acquisition or specified capital investment. The template resolutions, considered good practice by investors, were published in May 2016, with an expectation that they would be used at annual general meetings (AGMs) held after 1 August (and before that date where possible).
5. This report looks at the implementation of the Statement of Principles and the use of the template resolutions for meetings held between 13 March 2016 and 1 February 2017. It has been developed using information sourced from the Manifest Information Services Ltd

database¹, Thomson Reuters Practical Law's 'What's Market' database, public filings on company websites and other sources such as the London Stock Exchange.

6. The FRC would like to thank the members of the PEG for giving their time to the work of the group.

¹ Manifest Information Services Ltd holds data on most but not all companies listed on the Main Market. In addition, the PEG has overlaid its own definitions and interpretations of the information provided.

Monitoring of market practice

FTSE 350

REQUESTS FOR AUTHORITY TO ISSUE OR ALLOT					
Resolutions		Approved	Rejected	Withdrawn	
GENERAL TOTAL: 343 To approve a general authority to the directors to issue shares (331) Other Resolutions: - Allot or issue in relation to regulatory securities (12)		343	0	-	
SPECIFIC TOTAL: 6 Resolutions in connection with: - placings (4) - share consolidation (2)		6	0	-	
REQUESTS FOR AUTHORITY TO DISAPPLY PRE-EMPTION RIGHTS					
Resolutions	Authority for disapplication up to five per cent	Authority to disapply on shares constituting over five per cent	Approved	Rejected	Withdrawn
GENERAL TOTAL: 294 To disapply pre-emption rights on the issue of shares (290) Other Resolutions: - to disapply in relation to regulatory securities (4)	294	197 in the FTSE350 After 13 May: 141 Between 13 May and 1 August: 53, of which 16 used the two resolution format (all AGMs held in July) After 1 August: 32, of which 2 did not use template resolutions	293	1	2
SPECIFIC TOTAL: 3 Resolutions in connection with: - placings (3)	-	-	3	0	-

7. In the period covered by this report, two companies in the FTSE 100 and ten in the FTSE 250 raised funds non-pre-emptively. These issuances were all for less than ten per cent of the share capital, with six for less than five per cent. However, some of the issuances of more than five per cent appear not to abide by the Statement of Principles. When an additional five per cent disapplication authority is used, investors expect companies to disclose, in the announcement regarding the issue, the circumstances that have led to its use and to describe the consultation process undertaken. The PEG recommends that companies use the Statement of Principles as a framework for their discussions with companies and the template resolutions when proposing resolutions to disapply pre-emption rights. Companies not adhering to the expectations of the Principles are less likely to receive the support of their shareholders when putting forward subsequent disapplication requests. Best practice in engagement and disclosure is outlined in the appendix to this report.

8. As the table demonstrates, the template resolutions appear to have been well received. They have been widely used since the expected implementation date of 1 August, and were adopted by a number of other companies as best practice after their publication on 13 May. 197 companies in the FTSE 350 applied for a disapplication authority of more than five per cent in the relevant period. 64 FTSE 100 and 77 FTSE 250 companies respectively applied for authority to disapply more than five per cent after 13 May, when the template resolutions were introduced. 16 companies used the template resolutions before the expected implementation date of 1 August, all of which held their AGMs in July. However, after 1 August, two companies in the FTSE 250 applied for in excess of five per cent disapplication but used a 'one resolution' format, rather than the template resolutions. These two companies, Entertainment One and Vedanta Resources, applied for disapplications of up to ten per cent of their share capital within one resolution, although both mentioned the restrictions of the Statement of Principles in either the Chairman's statement or the explanatory notes.
9. Across the FTSE 350, resolutions for additional five per cent disapplication received less support than those covering the first authority. This may reflect concern about the proposed use of the additional disapplication authority and previous company issuance practices.
10. In most investors' opinion, an additional five per cent disapplication authority should only be proposed when appropriate for the company's individual circumstances. It appears that most of those organisations which had applied for ten per cent disapplication in the past did so again in this monitoring period. A number of companies did not apply for authority to disapply a second five per cent, but noted reasons for not doing so at their AGM. SAGE, for example, chose not to seek authority for the additional five per cent, but the Chairman's statement noted that it may be sought in the future. The statement read as follows:

"The directors are aware of the Pre-Emption Group's Statement of Principles, as updated in March 2015, and the template resolutions published in May 2016, and may, if considered appropriate, seek authority by way of an additional resolution at future Annual General Meetings to issue shares for cash on a non-pre-emptive basis up to an amount equal to a further 5% of the issued share capital of the Company, provided that such additional authority is used only in accordance with the Pre-Emption Group's Statement of Principles."
11. Two resolutions in the FTSE 350 were withdrawn in the monitoring period. Micro Focus International plc withdrew a resolution to disapply pre-emption rights on the issue of shares for cash for purposes of acquisitions or capital investments up to ten per cent. This limit was referenced within the resolution. It was proposed in addition to requests for the five per cent for general corporate purposes and a separate five per cent for specified capital acquisitions or investment. In the explanatory notes, the company stated:

“following discussions with certain shareholders and to enable the Company to be more competitive when negotiating transactions that create substantial shareholder value, the Company seeks shareholder approval in Resolution 20 to disapply pre-emption rights on an allotment in respect of up to a further 10% of the entire issued share capital of the Company (excluding treasury shares). The authority in Resolution 20 would also be limited to an allotment in connection with an acquisition or a specified capital investment. The board believes that approving this resolution is in the best interests of the Group, and the shareholders as a whole.”

12. In the FTSE 250, one authority to disapply pre-emption rights on the issue of shares for cash for use in acquisitions or other capital investments was withdrawn at Greene King plc. This authority requested an additional five per cent, and the resolution referenced the restrictions around use only to finance a specific acquisition or capital investment.
13. Only one resolution in the FTSE 350 was defeated, that of the general authority to disapply on the issue of shares for cash up to five per cent at SVG Capital. A poll was called on this special resolution, as opposed to the others, which were considered on a show of hands. The resolution received a ‘for’ vote of 68.01 per cent, an insufficient majority. Similar to last year, whilst the majority of resolutions received above 96 per cent support, those on the Remuneration Report and for the re-election of the SVG Capital CEO and Chairman also received less than 70 per cent support. SVG Capital published the following statement alongside the release of its AGM results:

“SVG Capital has a diverse shareholder base and the vote therefore reflects a range of views. The Board is mindful of the notable vote against four of the resolutions at this year’s Annual General Meeting. The Board notes that, similar to prior years, one large shareholder’s vote represented a very significant percentage of the vote against the respective four resolutions. Through the year the Board has engaged with our larger shareholders on remuneration and, in particular, notes the comments raised concerning disclosure of retrospective bonus targets. The Board will seek to address these comments in future reports. We look forward to continuing an open and constructive dialogue with shareholders.”

14. Disapplication resolutions are subject to the special resolution threshold. In keeping with Provision E.2.2 of the UK Corporate Governance Code when, in the opinion of the board, a significant proportion of votes has been cast against a resolution at any general meeting, the company should explain, when announcing the results of voting, what actions it intends to take to understand the reasons behind the vote result.
15. A significant majority of FTSE 350 resolutions covering authority to issue or allot shares or disapply pre-emption rights were addressed at AGMs. Only six FTSE 350 resolutions concerning authority to issue or allot shares or disapply were addressed at Extraordinary

General Meetings. Another 15 resolutions were considered at GMs and there was one class-specific meeting of ordinary shareholders.

16. The greatest number of requests for issuance or to disapply pre-emption rights came from financial sector companies (263), with requests for authority broadly reflecting the sectoral composition across the index.

FTSE Small Cap

REQUESTS FOR AUTHORITY TO ISSUE OR ALLOT					
Resolutions			Approved	Rejected	Withdrawn
GENERAL TOTAL: 259 To issue shares (241) Other Resolutions: - to issue in respect of an open offer/placing (7) - to issue in relation to capital reclassification (3) - to issue at a discount (2) - to issue in connection with specific placing (6)			259	0	0
SPECIFIC TOTAL: 2 Resolutions in connection with: - mergers (2)			2	0	0
REQUESTS FOR AUTHORITY TO DISAPPLY PRE-EMPTION RIGHTS					
Resolutions	Authority for disapplication up to five per cent	Authority to disapply on shares constituting over five per cent	Approved	Rejected	Withdrawn
GENERAL TOTAL: 200 To disapply on the issue of shares for cash (195) Other resolutions: - to disapply to allow a refinancing (2) - to disapply on a particular share class (3)	200	12	196	4	1
SPECIFIC TOTAL: 2 Resolutions in connection with: - a merger (1) - recapitalisation (1)	-	-	2	0	0

17. In the FTSE Small Cap, 12 companies raised funds non-pre-emptively. Only one of these authorities was below five per cent, with five granting between nine and ten per cent. A further six companies raised more than ten per cent of their capital, with one issuing 25 per cent, although this was an Infrastructure Income Fund.

18. In the FTSE Small Cap four resolutions were defeated, all relating to authorities to disapply. Two of these resolutions were proposed by John Menzies, with the other two put forward by Stock Spirits Group and Regional REIT Ltd.

19. At the John Menzies AGM in May 2016, two resolutions were defeated, one to disapply pre-emption rights and the other to allow meetings to be held on not less than 14 days' notice. Both of these were proposed as special resolutions, but received less than 60 per cent approval. At its general meeting of 11 October to approve the proposed acquisition of ASIG Holdings Limited and ASIG Holdings Corp, John Menzies again lost its resolution to disapply pre-emption rights, this time receiving less than 50 per cent support. Interestingly, the resolution to disapply pre-emption rights in connection with the issue of ordinary shares to Dr Dermot Smurfit, the Chairman, received more than 99 per cent support.
20. At its AGM, Stock Spirits Group also lost a resolution to disapply pre-emption rights, receiving 74 per cent approval rather than the necessary 75. This was a meeting at which four requisitioned resolutions were proposed, and three eventually put to shareholders. These resolutions covered the election of two new directors and support for a further review of merger and acquisition activity. All three of the shareholder proposed resolutions were passed, receiving between 54 and 56 per cent of the vote.
21. Regional REIT Ltd put forward a resolution to disapply pre-emption rights in respect of up to ten per cent of the issued share capital at its 2016 AGM. The pre-emption resolution did not pass, receiving 74 per cent support. On noting that it would engage with shareholders to understand the results, the Board also drew attention to another resolution which received a significant vote against, of 28 per cent. This resolution gave directors the authority to issue shares below net asset value, but passed as it required only a simple majority.
22. In the FTSE Small Cap, one resolution was withdrawn in the monitoring period. This resolution was put forward by Petropavlovsk plc and granted a general authority to directors to disapply pre-emption rights on the issue of shares for cash. The resolution did not follow the template, and instead included a reference to use in connection with a specified capital acquisition or investment in the Chairman's letter.

FTSE Fledgling

REQUESTS FOR AUTHORITY TO ISSUE OR ALLOT			
Resolutions	Approved	Rejected	Withdrawn
GENERAL TOTAL: 64 Authority to issue or allot shares (56) Other Resolutions: <ul style="list-style-type: none"> - to issue preference shares (1) - to issue at a premium to NAV (1) - to issue in connection with a capital raise (2) - to issue at a discount (2) - in relation to a share consolidation/reorganisation (2) 	62	2	0
SPECIFIC TOTAL: 1 <ul style="list-style-type: none"> - Resolution in connection with a placing 	2	0	0

REQUESTS FOR AUTHORITY TO DISAPPLY PRE-EMPTION RIGHTS					
Resolutions	Authority for disapplication up to five per cent	Authority to disapply on shares constituting over five per cent	Approved	Rejected	Withdrawn
GENERAL TOTAL: 64 To disapply on the issue of shares for cash (63) Other resolutions: - to disapply in relation to a capital raise (1)	61	3	63	1	0
SPECIFIC TOTAL: 1 Resolution in connection with a placing	-	-	1	0	0

23. Three companies in the FTSE Fledgling index applied for disapplications above five per cent. One of these companies, Treatt plc, applied for disapplication authorities in two separate resolutions, but did not include specific reference to use in connection with an acquisition or specified capital investment in the second resolution. The other companies applied for ten per cent in one resolution, and more than eight per cent in another, although the second of these was put forward by an Investment Trust. The template resolutions illustrate an approach which investors consider to be good practice, and the PEG recommends companies use the template resolutions when putting forward requests to disapply pre-emption rights.
24. In the FTSE Fledgling in the period covered by this report, four companies raised funds non-pre-emptively. Two of these were for between five and ten per cent of their share capital. Two further issuances were made by Aurora Investment Trust, for 16 per cent and 33 per cent of their share capital.
25. Once again, two resolutions in our monitoring period were defeated at JKC Oil and Gas plc. These resolutions, to issue shares and to disapply pre-emption rights, were defeated at the AGM in June. Only three of the 11 resolutions put forward at this meeting passed – those to re-appoint the auditors, to approve the auditors’ remuneration and to allow meetings to be held on not less than 14 days’ notice. The company issued a statement with the AGM results that ‘It is noted that the main shareholder voting against these resolutions was Eclairs Group Limited, the owner of 47,287,027 shares’.
26. Dee Valley Group’s resolution to allot shares was the other FTSE Fledgling resolution defeated in 2016. Dee Valley has since been the subject of an acquisition by Severn Trent Water Limited.

Issuances in other indices or listings

27. In addition, there were eight non-pre-emptive fund raisings carried out by London Stock Exchange listed companies, but these sat outside the indices we consider as part of our monitoring report. These placings varied greatly in size, from six per cent of share capital issued to over 100 in the case of Energiser Investments plc.
28. There were also nine issuances by AIM-registered companies in the relevant period, with many of these above the threshold suggested by the Statement of Principles. Companies admitted to the Standard Listing, High Growth segment or to trading on AIM are encouraged to adopt the Principles, but the Statement of Principles applies to those with a premium listing in the first instance.

Level of Support for Disapplication Authorities

29. We also analysed the level of support for disapplication authorities across the three indices. The following table covers defeated disapplication authorities, and also analyses the level of abstention and 'dissent', which combines abstentions and votes against. Companies of all sizes received significant support for their requests, evidenced by the small number of resolutions in this table in comparison to the level of disapplication requests.

Votes against, abstentions and dissent for resolutions covering disapplication by FTSE Index ²							
	10-15%	15-20%	20-25%	25-30%	30-35%	35-40%	>40%
Votes against							
FTSE 350	53	27	7	2	2	0	0
FTSE Small Cap	12	6	1	7	0	1	3
FTSE Fledgling	0	2	1	0	0	0	3
TOTAL	55	35	9	9	2	1	6
Abstentions							
FTSE 350	5	0	0	0	0	0	1
FTSE Small Cap	4	0	0	1	1	0	0
FTSE Fledgling	0	2	1	0	0	0	1
TOTAL	9	2	1	1	1	0	2
Dissent							
FTSE 350	61	37	11	2	1	1	1
FTSE Small Cap	16	5	3	5	3	2	3
FTSE Fledgling	0	4	2	0	0	0	4
TOTAL	77	46	16	7	4	3	8

30. There is a relatively low rate of abstention across these indices except in a few cases. There were a greater number of dissent and against votes of up to 20 per cent of the vote at the FTSE 350 level, such as the abstention of more than 25 per cent at the Lavendon AGM, where a ten per cent authority to disapply was proposed as one resolution, although before the template resolutions were introduced. Other notable results in the FTSE 350 include a company which received over 68 per cent dissent, composed of 67 per cent abstention and

² Note: Some companies do not provide detailed voting returns, so these statistics only reflect available records.

less than one per cent against. Two other companies with dissent greater than 20 per cent received 13 per cent abstention and eight against and eight per cent abstention and 15 against respectively.

31. In the FTSE Small Cap, two companies received abstentions of over 25 per cent – 27 per cent and 34 per cent respectively. Interestingly, Petropavlovsk plc also received dissent of over 40 per cent, but the resolution passed, as it required only a simple majority. Petropavlovsk also withdrew a request for disapplication authority at their AGM.
32. In the FTSE Fledgling, one company received more than 50 per cent dissent on a general authority to issue shares to a specific entity. There were also four abstentions of over 15 per cent on resolutions in the FTSE Fledgling, each of which received a vote against of less than one per cent.

Conclusion

33. This report demonstrates that the template resolutions and Statement of Principles have generally been adhered to, but examples of possibly poor consultation and disclosure in the monitoring period have been brought to the PEG's attention. It is important that discussions between companies and investors address both the spirit and letter of the Statement of Principles. It further demonstrates that a request for general disapplication is likely to be supported where it meets the criteria regarding size, duration and resolution format, but this does not reduce the importance of effective dialogue and timely notification.
34. The Statement of Principles is supported by representatives of listed companies, investors and intermediaries. Flexibility for companies to apply for an authority to issue non-pre-emptively in respect of two allocations of five per cent was provided in the 2015 Statement of Principles. The greater flexibility included expectations about specific use. The expectation is that regardless of the legal form of a transaction, companies will consider the thresholds, with the second five per cent specifically tied to acquisitions and specified capital investments. The investor view also remains that the additional five per cent should not be applied for automatically, but only when it is appropriate for the company's circumstances.
35. The focus of the Statement of Principles is early and effective consultation between investors and companies. Consultation about proposed issuances must be specific and unequivocal, and the topic of whether or not pre-emption authority is to be utilised must be explicitly addressed. Disclosure of the reasons for the issuance is also important. When utilising an additional five per cent authority, investors expect companies to disclose the circumstances that have led to its use and to describe in detail the consultation process undertaken.
36. In this context, companies which do not adhere to the Statement of Principles are less likely to receive ongoing shareholder support and should expect investors to question specific issuances that appear to be contrary to the Statement of Principles. Companies should also note that where they do not use the template resolutions this may form part of an advisor's rating analysis.
37. The use of the Statement of Principles will also be monitored by the PEG on an ongoing basis, particularly in light of regulatory changes surrounding implementation of the Prospectus Regulation.

APPENDIX OF BEST PRACTICE IN ENGAGEMENT AND DISCLOSURE

Applying for disapplication authority

- The template resolutions provide for companies to propose separate resolutions to authorise companies to:
 - o disapply pre-emption rights on up to five per cent of the issued share capital; and
 - o disapply pre-emption rights for an additional five per cent for transactions which the board determines to be an acquisition or other specified capital investment as defined by the Statement of Principles.
- Investors consider that the additional five per cent disapplication authority included in the template resolutions should only be proposed when appropriate for the individual company's circumstance.

For an issuance

- Companies should, where possible, signal an intention to undertake a non-pre-emptive issue at the earliest opportunity and to establish a dialogue with the company's shareholders.
- Consultation about proposed issuances, including that the issuance is taking advantage of the additional five per cent authority for acquisitions or other specified capital investment, must be specific and unequivocal to be considered appropriate. Such consultation should be with a wide range of shareholders.
- Shareholders should, where possible, engage with companies to help them understand the specific factors that might inform their view on a proposed disapplication of pre-emption rights by the company. They should review the case made by a company on its merits and decide on each case individually using their usual investment criteria.
- When an additional five per cent disapplication authority is used, companies should disclose, in the announcement regarding the issue, the circumstances that have led to its use and describe in detail the consultation process undertaken.
- Issuers are reminded that any issuance in excess of the general disapplication resolution of five per cent will only be within the ambit of the Statement of Principles if it is in connection with an acquisition or specified capital investment. Issuance in excess of five per cent of ordinary share capital for other reasons is not consistent with the ambit of the Statement of Principles. This includes, but is not limited to, and issuance by way of a 'cashbox' placing.
- Companies will be expected to disclose any discount at which equity is issued in the announcement of the pricing of the relevant issue. Companies' attention is drawn to the guidance on calculation of discounts for these purposes in the Appendix to the Statement of Principles.

The next Annual Report and Accounts after issuance

- Companies are expected, where they have undertaken a placing using the disapplication of pre-emption rights, to publish in the next annual report:
 - o the actual level of discount achieved;
 - o the net proceeds raised;
 - o how those net proceeds were used; and
 - o the percentage increase in issued share capital due to non-pre-emptive issuance for cash over the three-year period preceding the issue.

The Pre-Emption Group advises that companies which do not comply with the letter and spirit of the Statement of Principles are likely to find their shareholders less inclined to approve subsequent requests for disapplication.

The Statement of Principles provides a framework for engagement between companies and investors. Disapplication requests mirroring the size, duration and resolution format outlined in the Statement of Principles and this document are likely to be well supported by shareholder. However, effective dialogue remains the cornerstone of the Statement of Principles and companies and investors should use this framework to begin such discussions.

Contacting the Pre-Emption Group

Any comments on this report, and any other correspondence, should be addressed to the Secretary of the Pre-Emption Group. Her contact details are:

secretary@pre-emptiongroup.org.uk

or write to:

Hannah Armitage
Secretary, Pre-Emption Group
Financial Reporting Council
8th Floor
125 London Wall
London EC2Y 5AS