Editorial

Corporate Law and Finance in 1994 – A Busy Year

Even by modern standards, 1994 was a hyperactive year in the field of corporate law and finance. This article rounds up the year's key City developments – many of which will run and run into 1995 and beyond.

The London Stock Exchange

New Rules for the USM
A new Unlisted Securities Market Rulebook took effect from 30 June 1994. This closely followed the revised Listing Rules introduced in late 1993 for listed companies, and thus considerably tightened the previous USM requirements. Particular new requirements included:

- Cadbury Code compliance statement in annual reports;
- Stricter requirements on disclosure and display of directors' service contracts;
- Stricter Model Code for directors' share dealings;
- Directors' declarations of business interests at least every three years.

New Rules and Regulations for Member Firms
A new rulebook was also issued for member firms of the Stock Exchange – market makers, brokers and other market participants. The main changes were in the areas of compliance and discipline, although of more interest to lawyers was the disappearance of the time-honoured reference to "listing becoming effective in acordance with Rule 520".

Rolling Settlement Introduced
In July, the old account-based settlement system was scrapped, and all trades in shares of UK companies were required to be settled 10 days after trading – T + 10. The plan is to move to T + 5 in time for the introduction of CREST in 1995/1996.

Dissemination of Price Sensitive Information
Guidance, effective from 1 March 1994, was issued on the dissemination of price sensitive information by listed companies. The guidance was in two main sections:

- Defining price sensitive information and the ongoing systems which companies should have in place to evaluate, safeguard and if necessary announce it;
- Dealing with a number of specific situations and issues which come up repeatedly. Particular prominence was given to handling relationships with analysts and the press, observing the principle that companies should take great care to ensure that all investors are equally well informed.

Access to Capital for Smaller Companies - AIM
The Stock Exchange was at pains to ensure that the requirements for capital of smaller, as well as larger, companies were catered for. A seven-point plan was launched, featuring a number of initiatives and liaison devices. The most ambitious, however, was the proposed Alternative Investment Market, intended to replace the USM at the end of its planned life in 1996.

AIM is proposed to be a development of the Rule 4.2 (the old Rule 535.2) matched bargain trading facility. Under the initial proposals, which attracted some criticism for being insufficiently rigorous, companies applying to join AIM would have to publish a prospectus, although it would not be vetted by the Exchange. Neither would companies *have* to appoint a sponsor, although they could if they wanted to. The intention was to make it cheaper for companies to come to AIM than to the Official List.

Short Selling and Dealings ahead of Price Sensitive Information
The year closed with two consultative papers on how to tackle alleged market distortions:

- Short selling – where the seller does not actually own the stock he contracts to sell – can drive down market prices if carried out on a large scale. This is a particular concern during secondary offers such as Wellcome and BTs 2 and 3. Although the Exchange's investigation failed to turn up much hard evidence of short selling, it did advance a number of possible counter-measures, such as forced disclosure or compelling short sellers to disgorge profits.
- Dealings ahead of price sensitive information – concern was expressed about a number of instances where it turned out that a company's shares had moved sharply just before price sensitive information was announced, giving rise to an inference of insider dealing. The Exchange proposed counter-measures, involving the monitoring of price movements: when a price movement breached pre-set parameters, the Exchange would issue an alert and investigate. If the investigation showed evidence of insider dealing, trading might be suspended pending an announcement. The proposed trading suspension has attracted widespread criticism.

Insider Dealing - a New Regime

The new insider dealing regime under the Criminal Justice Act 1993 came into force on 1 March 1994. Changes included:

- No connection now required between primary insider and issuer of price-affected securities;
- All dealings involving a professional intermediary now caught, even if off-market;
- Dealings in municipal and sovereign securities (eg gilts) are now within the legislation;
- Derivatives are within the new law if they themselves are traded on a relevant market, or if the underlying securities are so traded.

CREST Developments

The Bank of England working group continues to develop CREST, the project for a paperless securities transfer system which was set up in the wake of the failure of Taurus. A Legal Issues paper was published, following which it is expected that the draft CREST Regulations will be issued in early 1995.

Fixed and Floating Charges: *New Bullas, GE Tunbridge* and *Griffiths v Yorkshire Bank*

Cases involving priorities between successive fixed and

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floating charges are always something of a lottery:

- In *Re New Bullas Ltd* [1994] BCC 36, the Court of Appeal focused on the intention of the parties rather than the construction of the debenture. The debenture purported to create a fixed charge over present and future book debts, although the company was to be free to deal with the book debts unless it received specific instructions from the chargee. Rejecting the argument that this freedom meant that the charge was in reality a floating one, the Court of Appeal upheld the parties' right to contract on whatever terms they chose, unless their agreement contravened established precedent.
- In *Re GE Tunbridge Ltd* [1994] BCC 563, by contrast, the court looked solely at the wording of the debenture. Again, the question was whether a charge over present and future assets was, as it purported to be, a fixed charge, or, in view of the fact that the company would inevitably deal with the assets in the course of its business, a floating charge. In this instance, the court held that a floating charge had been created.
- In *Griffiths v Yorkshire Bank* [1994] 1 WLR 1427, the company had granted two successive floating charges, even though the first charge contained a negative pledge by the company not to create further charges. The second floating charge crystallized before the first. The court held that the second charge had priority, despite the negative pledge, the only effect of which was to give the first chargee a possible right of action against the company for breach of contract.

Financial Law Panel: Netting and Security over Cash Balances

The Financial Law Panel's first pronouncement was a statement of the current state of English law on netting – the ability of banks to set off credit and debit balances upon the insolvency of a customer. Although breaking no new ground, the exercise was valuable in that it was endorsed by leading City law firms.

Later in the year, the FLP considered the *Charge Card* decision – that it is not possible for a bank to take a charge over a customer's deposit on the bank's own books. The FLP recommended that "properly drawn contractual set-off terms will provide satisfactory security to a bank or other institution over a debt which it owes", and, therefore, that other security devices could be omitted from security documentation. However, the FLP added the cautionary note that its recommendation applied "save in exceptional circumstances", which it did not specify.

The FLP also issued a valuable paper on Shadow Directorships.

The Local Authorities in the Courts

- The long shadow of the *Hammersmith* ([1991] 1 All ER 545) decision was apparent in *Westdeutsche Landesbank Girozentrale v Islington LBC* [1994] 1 WLR 938. This was a good result for the bank: not only was it able to recover money paid to the local authority under a swap contract, but it was also entitled to compound interest on the amount repaid;
- Less satisfactory, from the banker's point of view, was the Scottish decision in *Morgan Guaranty v Lothian RC* (The Times, 30 November 1993), where the court also found a swap contract entered into by a local authority *ultra vires* and unenforceable, but, unlike the English court, refused to order the local authority to repay money it had received to the bank;
- Also worrying for lenders was *Credit Suisse v Allerdale BC, The Independent*, 17 June 1994, where the local authority guaranteed a loan to its wholly owned development company. Reviewing the local authority's statutory powers and functions, the court held that the giving of the guarantee was *ultra vires* and it was therefore unenforceable.
- However, the year finished on a happier note for Credit Suisse, when it succeeded in enforcing a local authority's guarantee in litigation against *Waltham Forest LBC* [1994] NPC 137.

Money Laundering

The new money laundering regime, under the Criminal Justice Act 1993 and the Money Laundering Regulations, came into force on 1 April 1994.

In addition to specific money laundering offences of:

- acquiring, possessing or using proceeds;
- assisting;
- tipping off; and
- failing to report

there are obligations on financial and investment businesses to introduce anti-money laundering procedures covering:

- identification, record-keeping and internal reporting;
- prevention;
- education and training.

At last ... the Prospectus Directive

Finally, the Treasury announced revised plans for the implementation of the Prospectus Directive, to govern offers of unlisted securities in the UK. Part V of the Financial Services Act 1986 will not, after all, be brought into force – instead there will be new Regulations, under the European Communities Act, expected to come into force during 1995.

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