

SHARE CAPITAL MANAGEMENT GUIDELINES

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The Investment Association is a company limited
by guarantee registered in England and
Wales. Registered number 04343737.

Following the merger of ABI Investment Affairs with the IMA on 30th June, 2014, the enlarged Investment Management Association (IMA), which was renamed The Investment Association in January 2015, has assumed responsibility for guidance previously issued by the ABI.

This guidance sets out the expectations of The Investment Association's members as institutional investors on various aspects of share capital management. It applies to companies whose shares are admitted to the premium segment of the Official List of the UK Listing Authority.

Companies whose shares are admitted to the standard segment of the Official List, to trading on AIM, or to the High Growth Segment of the London Stock Exchange's Main Market, are encouraged to adopt this guidance.

1 Directors' Power to Allot Shares

This sets out the expectations of Investment Association members where companies seek shareholder authorisation for the general allotment of new shares and any disapplication of pre-emption rights.

The ABI guidelines on directors' powers to allot shares were last revised in January 2009 following a recommendation by the Rights Issues Review Group to the Chancellor that the ceiling on allotments of shares should be increased from one-third to two-thirds of the issuer's share capital. This has generally functioned well.

1.1 Section 551 – General Power to Allot

- 1.1.1 Members will regard as routine an authority to allot up to two-thirds of the existing issued share capital. Any amount in excess of one-third of existing issued shares should be applied to fully pre-emptive rights issues only.
- 1.1.2 This routine authority is acceptable as appropriate protections against shareholder dilution are provided both by pre-emption rights and the requirement that shareholders of premium listed companies in the UK have a vote on all major transactions – under Listing Rule 10.5, a listed company must, in relation to a Class 1 transaction send an explanatory circular to its shareholders and obtain their prior approval in a general meeting for the transaction / ensure that any agreement effecting the transaction is conditional on that approval being obtained.
- 1.1.3 The authority should be approved by ordinary resolution and be for the period until the next Annual General Meeting.
- 1.1.4 In calculating existing issued share capital, any shares held in Treasury should be excluded.

1.2 Section 570 – General Power to Disapply Pre-emption Rights

- 1.2.1 The terms of a special resolution to disapply pre-emption rights should comply with the provisions of the Pre-emption Group's current Statement of Principles.
- 1.2.2 The Investment Association notes that the Pre-emption Group has provided [template resolutions](#) for the disapplication of pre-emption rights. The template provides for two separate resolutions, which relate to:
- a) Disapplication of pre-emption rights on up to five per cent of the issued share capital to be used on an unrestricted basis; and
 - b) The second resolution, to be put forward by companies when appropriate, requests the disapplication of pre-emption rights for an additional five per cent in cases when boards consider the use to be for the purposes of an acquisition or specified capital investment in accordance with the Statement of Principles.
- 1.2.3 Investment Association members' are supportive of this update and expect that any company seeking a disapplication of pre-emption rights which in aggregate is equal to 10% of the issued capital to follow the model resolutions.
- 1.2.4 Investment Association members have asked the Institutional Voting Information Service (IVIS), the IA's corporate governance research service, to take the following approach for companies seeking a disapplication of pre-emption rights which in aggregate is equal to 10% of the issued share capital:
- a) From **1 August 2016**, IVIS will amber top any company which does not provide two separate resolutions as set out in the template.
 - b) From **1 January 2017**, IVIS will red top any company which does not provide two separate resolutions as set out in the template.

2 Own Share Purchase

Institutional investors are supportive of companies' efforts to return surplus funds to shareholders. Dividend payments remain the preferred method for regular distributions to shareholders. However, the following guidelines are provided for companies who decide that share repurchases are in the best interests of their shareholders.

2.1 Authority to Repurchase Own Shares

- 2.1.1 Companies should seek authority to purchase their own shares whether on market or off market by special resolution and not simply an ordinary resolution as is allowed by Sections 694 and 701 of the Companies Act 2006.

- 2.1.2 A general authority to purchase shares should be renewed annually.
- 2.1.3 Shareholders expect that a general authority for a company to purchase its own shares will be exercised only if it is in the best interests of shareholders generally and normally only if it would result in an increase in earnings per share or, in the case of property companies and investment trusts, if it would result in an increase in asset value per share for the remaining shareholders. Where this is not expected, the benefits should be explained clearly.
- 2.1.4 Companies should disclose in their next Annual Report the justification for any own share purchases made in the previous year, including an explanation of why this method of returning capital to shareholders was decided upon. In this context, companies should discuss the effect share buybacks have on earnings per share (EPS), total shareholder return (TSR) and net asset value (NAV) per share. EPS and TSR targets under both short and long-term incentive schemes should take account of the effect of share buybacks. Market conditions should be carefully considered and an average price paid should be disclosed. The effect on the holdings of major shareholders might also merit discussion in the Annual Report.

2.2 Amount

- 2.2.1 A general authority to purchase up to 10% of the existing issued Ordinary share capital is unlikely to cause concern.
- 2.2.2 The Institutional Voting Information Service (IVIS) will note a general authority to purchase more than 10% (but less than 15%) of the existing issued ordinary share capital. A repurchase of more than 15% is not permitted under the Listing Rules, unless carried out by a tender offer.
- 2.2.3 In calculating existing issued share capital, any shares held in Treasury should be excluded.
- 2.2.4 Whilst the Companies Act now allows companies to hold more than 10% of their shares in Treasury, the Investment Association's preference is for companies not to hold more than 10% in Treasury.

2.3 Price

- 2.3.1 Investment Association members consider as appropriate the requirement of the Listing Rules that (unless a tender offer is made to all shareholders) purchases of less than 15% of the issued share capital pursuant to a general authority should be at a price which does not exceed the higher of:
 - a) 5% above the average market value of the company's shares for the five business days before the purchase is made; and
 - b) the higher of the price of the last independent trade and the highest current independent bid on the market where the purchase is carried out.
- 2.3.2 Members discourage share buybacks that are done off-market unless there is transparency on terms and pricing.

2.4 Dealings by Companies in Derivatives over their Own Shares

- 2.4.1 Investors are concerned about unusual structures and transactions that relate to returns of capital where there might be unusual risks.

- a) The boards of companies contemplating returns of capital through contingent dealings in their own shares, or in derivatives referenced to their shares, should explain these clearly to shareholders and demonstrate the expected benefits to, and safeguards for, shareholders.
- b) Prior authority for any such dealings should be sought and approved via a specific special resolution and the amount should be counted within the general authority limit.
- c) Companies should report in due course on the effectiveness and benefits of any such dealings in their next Annual Report.

3 Scrip Dividends

- 3.1.1 Investment Association members are concerned about the dilutive effects of scrip dividend issues. Consequently, they normally prefer that shares offered in lieu of dividends are sourced from shares purchased in the market (Dividend Reinvestment Plans or "DRIPs"), rather than primary issuance.
- 3.1.2 However, in some circumstances, shareholders may be offered an option of taking newly issued shares in lieu of a dividend.
- 3.1.3 Any authority to offer a scrip dividend using new shares should be renewed at least every three years.
- 3.1.4 Shares to the value of the cash dividend forgone should be allocated at the average of the middle market quotations on the London Stock Exchange, as derived from the Daily Official List, for the five business days beginning on the ex-dividend date.
- 3.1.5 Arrangements whereby a scrip dividend offer is cancelled are only acceptable if a clear rationale and explanation to shareholders is provided.

4 Issuance of Shares by Investment Trusts

- 4.1.1 New shares should not be issued below net asset value (NAV).
- 4.1.2 Treasury shares should only be re-issued at a discount which is lower than the weighted average discount at which all shares held in Treasury have been repurchased.
- 4.1.3 Boards should always explain why they believe it is in the interest of shareholders to hold shares in Treasury for potential re-issue at a discount rather than to cancel them at the time of re-purchase.

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