

Insights

FCA REVIEW OF SPONSORS REQUESTS: IDENTIFYING AND MANAGING CONFLICTS

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SUMMARY

The FCA has published Primary Market Bulletin No.37 (PMB) with the findings of its review of conflict queries since the publication of Technical Note 701.3. In general, there have been fewer conflict queries but the review highlighted a few cases of interest where sponsors took action to reduce the risk of an actual or perceived conflict of interest, following discussion with the FCA. For example, where a senior employee of the sponsor firm was a member of the lending and sponsor team.

PMB No.37 reminds sponsors to use the reasonable market user test to help assess circumstances where a perceived conflict of interest exists and to contact the FCA early on if there are any unusual, novel or complex features to the transaction.

Background

In August 2017, the FCA published Technical Note 701.3 containing guidance on how the FCA expect sponsors to assess conflicts. If either no conflict exists or the firm can manage the conflict, the FCA would not expect a sponsor firm to contact them. However, a sponsor should contact the FCA if there are certain exceptional circumstances including:

- where the size of a proposed loan is greater than 0.5% of the sponsor group's total assets; or
- in the context of a related party transaction, a sponsor proposes to provide a fair and reasonable opinion and is also acting in another capacity, such as providing acquisition finance, for the related party or other party to the transaction.

Results of the FCA's review

- The majority of sponsors have not submitted a conflict guidance request since the introduction of Technical Note 701.3 and the overall number of conflict queries has decreased.

- Sponsors' submissions generally met the requirements in the FCA guidance.
- The most common types of sponsor conflict queries involved class 1 disposals/ acquisitions and IPOs.

Cases of interest

PMB No.37 highlights cases of interest where, following discussion with the FCA, a different course of action was taken to reduce any risk of a conflict. These include:

- Where a senior employee of the sponsor firm was a member of the lending team and the sponsor team. Following a discussion with the FCA, the firm removed the individual from the sponsor team to ensure that the teams could carry out their roles independently of one another.
- Where a sponsor firm provides loan finance through margin loans and takes collateral in the form of equity in the issuer. This could result in the firm having a material equity interest in its client that can be increased if the issuer is experiencing financial difficulty. Where the risk of the sponsor having a material equity interest is low, the guidance in TN 701.3 should be followed. However, sponsors should contact the FCA if there are any unusual, novel or complex features to the transaction or the sponsor's involvement in it.
- A sponsor provided a fair and reasonable opinion on a related party transaction at a time when the sponsor had been invited by the related party to provide acquisition financing for the transaction. The FCA were concerned that a conflict of interest or a perception of a conflict existed and so the issuer instructed another sponsor to provide the confirmation. Due to the importance of the sponsor's confirmation in these type of situations, the sponsor should contact the FCA before deciding if it can provide sponsor services.

Points to take-away

- A sponsor firm should provide its own analysis with its conflict submission.
- Sponsors should use the reasonable market user test to help assess circumstances where a perceived conflict of interest exists.
- Engage with the FCA early on.
- Contact the FCA if there are any unusual, novel or complex features to the transaction.

Primary Market Bulletin No. 37

Technical Note 701.3

RELATED CAPABILITIES

- M&A & Corporate Finance
- Securities & Corporate Governance
- UK Public Company

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