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FTSE Announces Change to Minimum Free Float Requirements

On December 14, 2011, the FTSE Group published the results of its market consultation on the minimum free float[1] requirements for inclusion of premium London-listed companies[2] in the FTSE UK Index Series – one of the most recognized indices in the world, which includes the FTSE 100 Index. The key outcome of the consultation is that, as of January 1, 2012, the minimum free float required for UK-incorporated companies will increase from 15% to 25%, with grandfathering of existing FTSE companies until January 1, 2014.

I. Current Free Float Requirements

Under the FTSE Ground Rules, companies that wish to be included in the FTSE UK Index Series must maintain a minimum free float:

- of at least 50%, if not incorporated in the UK; or
- of at least 15% (or 5% where the relevant company's market capitalization exceeds US $5 billion), if incorporated in the UK.

II. New Free Float Requirements

On December 14, 2011, FTSE published the results of its consultation on free float requirements and announced the following changes:

- the minimum free float required for UK-incorporated companies will rise from 15% to 25% from January 1, 2012 (this will mirror the 25% free float requirement that already applies to companies under the UKLA listing rules);

1 "Free float" means shares in public hands, which excludes, for example, shares held by significant shareholders and company directors.

2 Standard London-listed companies, including companies with GDR listings, are not eligible for inclusion in the FTSE UK Index Series.

- the new 25% threshold will not be waived by FTSE, even in cases where the UK Listing Authority has granted a waiver in respect of the 25% free float requirement under the UKLA listing rules; and

- existing FTSE companies with a free float of less than 25% will have until January 1, 2014, to increase their free float to 25%.

FTSE will undertake a further consultation on whether (i) an even higher threshold would be appropriate for UK companies, e.g. 50% (which would align free float requirements for UK and non-UK companies); and/or (ii) whether additional corporate governance standards should be incorporated into the Ground Rules.

III. Commentary

The consultation on free float requirements was launched in response to investor concerns that companies with small free floats afford too much influence to controlling shareholders, whose presence is often perceived to lead to poor corporate governance. These concerns are predominantly directed at foreign businesses that have incorporated (or plan to incorporate) a UK holding company to avoid having to dilute a controlling shareholder below a majority holding – as stated above, UK companies can have a much smaller free float and still enter the FTSE UK Index Series.

Certain market participants have questioned the validity of these concerns in the following terms:

- the conflation between a controlling shareholder and poor corporate governance standards is inaccurate;

- the view that the presence of a controlling shareholder in a non-UK company (or a non UK business with a UK holding company) is more problematic from a corporate governance perspective than in a UK company is misguided; and

- if there are genuine concerns regarding controlling shareholders and/or poor corporate governance standards in FTSE companies, the free float requirement is a blunt instrument with which to address these concerns, and there are more direct methods available.

While a 25% free float requirement is unlikely to result in any seismic shift in listing considerations for IPO candidates, the suggestion of a possible future with an even higher free float requirement for UK companies will continue to be a cause for concern for many market participants.

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If you would like to discuss any of the above issues further, please feel free to contact any of your regular contacts at the firm on +44 (0) 207 614 2200 or any of our partners and counsel listed under Capital Markets in the "Practices" section of our website (http://www.clearygottlieb.com).

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