Joint Listing Authority Advisory Panel (LAAP) and Markets Practitioner Panel (MPP) Response to CP21/21: Primary Markets Effectiveness Review

LAAP is an independent non-statutory panel that advises the FCA on policy issues which affect issuers of securities, and on policy and regulation proposals from the FCA listings function. Similarly, MPP is an independent statutory panel that the FCA is required to establish and maintain under FSMA. It advises the FCA on policy issues, regulatory proposals and other strategic matters that are likely to affect wholesale financial markets. The FCA Board appoints Panel Members and not as representatives of any individual firm; they are expected to contribute to the respective Panels from the perspective of wholesale and securities markets or the primary market sub-sector in which they are working, drawing on their personal experience and industry sentiment more generally.

This joint response reflects views widely held by LAAP and MPP Members and does not necessarily imply unanimity.

Q1: Would a single segment for equity shares in commercial companies meet the needs of both issuers and investors?

Q2: Which elements of the existing listing regime would you consider it most difficult or least desirable for issuers and/ or investors to operate without? Are there any particular elements you would reinstate? i.e. the controlling shareholder regime, or the free float requirements

Q3: Would the role of the sponsor be a significant loss? Is their role under any specific element of existing requirements considered significantly beneficial to issuers or investors currently?

Q4: What would be the benefit of being admitted to the Official List rather than just admission to a trading venue?

Q5: Should we have a role in approving the admission criteria set by trading venues and/or indices? Could adequate investor protection be maintained if different trading venues compete on admission requirements?

Q6: What types of issuers would find it hard to comply with the standards within the existing premium listing segment and why?

Q7: Do unlisted markets provide a suitable alternative to listed markets? Would a gap emerge for any particular type of issuer? Do you consider there would be any particular benefits or drawbacks to this approach?

Q8: What types of companies or strategies should the 'alternative' segment be aimed at?

Q9: Do the existing provisions in the standard segment need to be changed to suit these companies, either through relaxation or to provide additional shareholder protections?

Q10: How important is our role in setting additional admission standards to listing in the 'alternative' segment? Are there any benefits to this role being performed by us rather than a trading venue, or market discipline?

Q11: Do you consider the alignment between admission to the index and admission to the 'senior' segment to be important? Should the indices consider setting more objective admission criteria?

Considering the significant overlap between several of the questions in the CP, the response groups a number of questions together and answers them thematically rather than individually.

Firstly, LAAP and MPP would like to note that they consider this a bold consultation and commend the FCA for launching it and for its breadth of vision. The Panels of course recognise that amending the Listing Rules is only one element of the wider listing ecosystem and that this needs to be considered as a whole to ensure the competitiveness of London's offering as a listing venue and international financial centre.

In terms of the specific subject area of the consultation, the Panels believe that there is merit in simplifying the existing Listing Regime and creating a single segment for equity shares in commercial companies. They note that there is no super-equivalent regime in many other listing jurisdictions with which London competes. A single segment would contain common standards that would apply to established and growth companies, incorporated in the UK as well as overseas, within an overarching legislative framework.

This conclusion is driven by the view that the current division between the premium and standard listing segments is confusing for market participants and results in one of the two segments inevitably, and regardless of branding, being perceived as a 'second choice' venue. It also fails to clearly apportion the value which issuers derive from meeting this higher standard beyond index inclusion from the additional governance requirements comparative to other markets.

As currently constituted, standard is the only available option for some types of company that should be choosing London for their listing - for example, due to their growth characteristics in the track record period or going forward or free float. Furthermore, the higher standards of the premium listing segment as currently constituted, both at the eligibility stage and post-listing, are in some respects excessively onerous and operate as a competitive disadvantage when put side by side with other listing venues with which London competes. It is also not clear that there is any longer a meaningful or any uplift at all in valuation for issuers as a result of seeking a premium listing in London as opposed to listing on, in particular, continental European listing venues. This is important as the consideration by an issuer of which listing venue to choose is driven in large part - although not exclusively – by valuation.

It would be preferable to introduce a single, unified segment with specific chapters within that segment applying tailored rules to companies in particular sectors (such as mineral, scientific research based, high growth etc), along the lines of the separate chapters that were a feature of the listing regime before the division into premium and standard. It would not be appropriate to distinguish between UK and non-UK issuers in this context as creating additional hurdles for entry to listing for overseas companies would be contrary to the overall aim of maintaining and enhancing London as a competitive listing venue and international financial centre.

The preference for a single segment does not however necessarily mean abandoning the requirements of the premium listing segment in their entirety and a wholesale adoption of the rules of the standard listing segment. Reform needs to be carefully balanced with the need for appropriate governance standards, in particular recognising that some investors are active and some passive.

The Panels do believe however that there should be a careful review of the existing premium segment to retain only those elements that are of real value to investors or issuers. For example, elements of both the controlling shareholder and the related party regimes may well be worth retaining in a separate chapter. These regimes should nevertheless be looked at with fresh eyes and probably recast in simplified form as they

are currently overly complex and could have a greater degree of a disclosure-led regime. In terms of areas that would benefit from significant reform or even scrapping altogether, the significant transactions regime would be an example. As a result of the conditionality that is introduced into significant transactions by this approval requirement, as the FCA knows, a competitive disadvantage is created for premium listed companies that is not seen in other markets and thus potential competitive disadvantage versus unlisted or non-UK listed competitors in acquisitions for UK premium listed issuers. In the view of the Panels, no investor protection gain outweighs this significant disadvantage.

With regard to the sponsor regime, which is obviously a key feature of the premium segment, to date it has operated as an effective way for the FCA to outsource some of the policing of the Listing Rules. However, the regime is little understood or even known about by investors, who ascribe little or no value to it as a result. Nevertheless, the regime serves to drive the shape and scope of the comfort package on certain transactions. Accountants, for example, look carefully at the Listing Rule obligations of sponsors in determining what comfort they will provide and to whom. Previous changes to the sponsor regime have seen this comfort adjusted to reflect amendments to the rules. Equally, there can be some focus on areas by sponsors given their own historic experience that in amalgamation make the process more difficult and onerous for potential new applicants. Whilst clearly there are some advantages to the accounting work undertaken for the sponsor declarations, it has become a 'sponsor' led exercise rather than its historical use where it was seen as adding value by the Board in their role as directors. Therefore, a regime where it is clear to directors and the sponsor, and of course investors, what exactly the 'bar' and consequently appropriate diligence for any statements made for new applicants would be helpful. This could also potentially be clearer in disclosure statements within documents rather than shrouded in some mystery in the sponsor declarations.

The sponsor regime in its current form is onerous and prescriptive and, as a consequence of both that and the pronounced liability regime, there is an increased reluctance among institutions to take on the role given the greater dependence on sponsor banks. Further, the sponsor regime is not a feature of many competitor listing venues and yet they are not generally considered to have deleterious governance standards. Individual trading venues are able to impose a requirement for a qualified adviser through their own rulebooks: the AIM Rules for Companies impose a requirement to appoint a Nomad, the HGS Rulebook imposes a requirement to appoint a Key Adviser and both AQSE Rulebooks impose a requirement to retain an AQSE Corporate Adviser. These roles are clearly defined in terms of the functions they perform for the benefit of issuers and investors.

Going forward there should be a more principles-based and simplified sponsor regime to further enhance the deal making effectiveness of UK plc. The FCA may consider applying the regime in limited and clearly defined circumstances where they provide value - for example, when a company is joining the market for the first time. In the event that a lighter touch sponsor regime is introduced or the sponsor regime is abolished altogether, in order to ensure that appropriate levels of diligence standards are maintained - including for example, with respect to working capital and financial position and prospects procedures - the FCA could publish guidance on its expectations in relation to these standards and the comfort that should be provided by advisers, including accountants.

It is worth noting that if the sponsor regime is abolished in its entirety, this will be likely to have a consequential effect on both the size and nature of the FCA as regulator. Ultimately, in deciding what form the regime should take going forward, it is in reality for the FCA to assess what value it as a regulator derives from the regime and therefore what form it considers it should take given the answer to the value question.

The baseline standards which would be applicable within the single listing segment could be built on and further developed with the optionality to adopt higher governance standards on a voluntary basis in addition to employing additional disclosure.

Index eligibility will of course necessarily need to be reviewed in this context upon the introduction of a single listing segment given that only premium listed issuers are eligible for FTSE UK index inclusion under current FTSE Russell policies.

Given the passive nature of index investors it makes sense that a section within a single segment is established under the FCA supervision and enforcement framework or disclosure in which issuers can comply on voluntary basis in order to meet any specific investor demand. Premium rules which will be result of the ongoing consultation can provide the basis for this separate chapter.

Q12: How can the process for listing debt and debt-like securities be improved for issuers without jeopardising investor protection?

The Panels see limited scope to improve the listing process for debt securities, with the exception of retail targeted securities as discussed below, as issuers are able to access international investors efficiently using the current regime. However, the FCA could explore streamlining the regulation of admission to listing with the regulation of admission to trading on a UK regulated market. The FCA may also want to consider if the prospectus regime and Listing Rules could be expanded to accept disclosure standards for other jurisdictions such as the EU or US as meeting the equivalent UK rules for listing. This could in turn allow for one disclosure document to be used for offerings in multiple jurisdictions and listing on multiple venues thereby offering flexibility when designing debt programme documentation for frequent issuers. The Panels would otherwise caution against any changes that aim to improve but have the impact of deterring international non-UK investors from participating in the London listed debt markets.

The Panels feel there is a case to incentivise issuers with equity listed on the premium segment (or complying with equivalent rules under the new one segment structure) to offer their bonds in lower denominations - for example, £1,000 - and in doing so increasing the range of fixed income investments available to retail investors. A premium segment company will typically have a large retail investor base that has invested in its shares via the secondary market and increasingly through the primary market. The pandemic has seen an exponential growth in retail trading with the technology driven disintermediation of traditional financial service providers and there appears to be a prospective sustainable market for lower denomination bonds.

However, the availability of bonds distributed to retail investors remains weak. Issuers and advisors generally point to the requirement to produce a retail prospectus and the effect of the 'retail cascade' requirements leading to potential future disclosure liabilities, along with the potential applicability of PRIIPs regime requirements and the need for compliance with MiFID product governance requirements, as some of the non-pricing related inhibitors to issuing bonds in smaller denominations. For well-regulated and larger companies, the Panels believe there is a strong argument for prospectus requirements to be simplified owing to the rich supply of information which already exists in the market about these issuers.

The use of technology could allow investors to digest information beyond the prospectus and more effectively participate in corporate events in the long term. Concerns around investors use of leverage and understanding risk could also be mitigated with the introduction of restrictions on the sale of certain securities to certain retail investors on a risk-based product by product basis. The FCA may therefore want to focus on how functional retail participation might operate.

Q13: Should there be a separate listing segment for debt and debt-like securities?

A single separate debt segment can help in ensuring that fixed income rules evolve according to the need of debt issuers and investors. Such a segment could have disclosure requirements which, whilst broadly consistent with those which apply to equity securities, are more tailored to debt. It will be important to ensure that a separate debt segment does not reduce international participation in the UK listed debt market. It will also be important to ensure that the quoted eurobond exemption from UK withholding tax continues to be available for debt securities listed on such segment.

Q14: Which particular elements of the listing regime could be tailored to improve their effectiveness for other types of securities? In what way?

The Panels do not have anything to add here.

Q15: Do issuers consider the process of admitting further issues to both the FCA and the trading venue to be burdensome?

Whilst the process can be duplicative, it is not particularly burdensome for issuers, but it may be helpful post Listing Review to clarify processes, particularly around block listings and other post-IPO listings. It would also be helpful to consider more generally whether the two different sets of rules could benefit from being streamlined.

Q16: Would the existing procedures conducted by trading venues to ensure issuers comply with their disclosure obligations (production of a prospectus) need to be enhanced if we were to cease admitting further issues to the Official List? What costs would be associated with these, if any?

A considered response to this question needs further detail in respect of the proposed regime for secondary issuances and the circumstances under which it is envisaged that a prospectus would be required. As a principle the venue or entity which sets out the content of the admission document should be responsible for approving it and determining when is one required. In any event, we would expect the FCA to continue to have a monitoring role to the extent a prospectus is required, but if it is envisaged that an alternative document can be produced for a secondary issuance, we consider that this process could instead be subject to the rules of the trading venues, which would be monitored by the FCA.

Q17: Are there any legal, regulatory or tax requirements that are connected with further issues being admitted to the Official List, that could not be maintained by further issues being admitted to a trading venue?

The Panels do not think so, although the point mentioned in the response to Q13 above relating to the continued availability of the quoted eurobond exemption from UK withholding tax for debt securities also applies here.

Q18: Do you agree with our rationale for introducing DCSS to the premium listing segment? Is there any additional evidence that we should consider?

See the answer to Question 19 below.

Q19: Do you foresee any limitations to our proposal if the weighted voting shares are unlisted?

The Panels agree with the rationale for introducing the DCSS to the premium listing segment, pending the adoption of a single listing standard within which the DCSS would be permissible. Issuers would be able to decide on the particular structure of DCSS that suited their needs – which may go further than the conditions to be applied to DCSS in the current premium segment, as issuers such as Deliveroo and Wise have recently done – with index providers then able to specify the criteria they may expect to see in order to permit index inclusion. On this basis, the Panels are supportive of the DCSS proposal, pending the potential introduction of a single listing segment.

Q20: Do you consider that a five-year sunset period for DCSS in the premium listing segment is the correct length to protect companies from unwanted takeovers? Please provide evidence for your answer.

See the response to Question 21 below.

Q21: Do you consider that the mechanism proposed will be effective in providing a deterrent to unwanted takeovers? Please give reasons for your answer and any possible alternatives.

There are precedents for longer periods in other markets, but the proposed period should provide adequate protection from unwanted takeovers.

Q22: Do you agree with the proposed controls around DCSS in the premium listing segment? Are there any additional controls that would make the regime more effective?

Yes. The Panels do not propose any additional controls.

Q23: Do you agree with our proposal to raise the minimum market capitalisation for companies seeking to list under standard and premium listing to £50m? If not, please state your reasons and indicate what alternative threshold may be more appropriate along with any supporting evidence. We also welcome views on whether we should consider setting out conditions under which we might modify the proposed rule on the new threshold, and if so, what criteria stakeholders think we could usefully consider.

No. While there is a valid rationale to increase the cap from the current threshold of £700,000, increasing it to £50m is a crude eligibility threshold that is likely to mean that smaller issuers cannot use the Official List, which will be harmful to the attractiveness of London as a listing destination and the establishment of a workable continuum between private and public equity – particularly, as evidence suggests that firms are remaining privately held for much longer periods. Companies below the £50 million market capitalisation threshold also benefit from a main market listing and the Panels believe that the proposed threshold would limit choice for companies (especially SMEs) at a time when there is a desire to make primary markets in London more effective and competitive. If the threshold is to be raised it should be to a much lower number than £50m.

Q24: Do you consider that the current level of market capitalisation for listed debt remains appropriate? Please give reasons for your answer.

The Panels consider that there are no concerns relating to the current level of market capitalisation in the context of debt listings and consequently that the current threshold of £200,000 should not be increased. Tax considerations remain key for listing debt, in

particular, the quoted Eurobond exemption for withholding tax. UK companies wanting to list debt for this reason should not be precluded through an issuance size limit, if also prepared to comply with current disclosure requirements under the Prospectus Regulation or Listing Rules,

Q25: Do you agree with our proposal to reduce free float to 10% and to remove current guidance on modifications? Please give your reasons.

Yes, the Panels agree given that the purpose of free float is liquidity rather than being a governance mechanic. In conjunction with this, it will of course be important that FTSE Russell reconsider their index inclusion criteria and as discussed in Lord Hill's Review, the ability to have a lower free float would make the London market more competitive and the market could then make its own decisions on liquidity post-listing.

Q26: Would you find information about issuers' free float level useful to inform investment decision-making?

No. Investors already have easy access to information that provides a much better indication of the level of liquidity in a company's shares – for example, information on the LSE website in relation to daily, weekly and monthly volume of shares traded, prices for individual trades, bid/ask spreads, where trades were conducted etc – and the burden on an issuer of publishing regular information about its free float (determined in accordance with the Listing Rules) would be disproportionate to the benefit.

If the event that such a requirement was to be introduced, there would be operational challenges for issuers in determining which registered holders are:

(i) members of the same group; or

(ii) acting in concert with each other - i.e. which shareholders fall into the category in LR 6.14.3(e).

In principle, an issuer may be able to obtain this information by sending out section 793 notices but this process can be cumbersome and expensive and, in any event, may not produce a full picture of the share register and/or of which shareholders are 'connected' to each other.

Q27: Do you agree with our proposal to leave track record requirements as they are now, based on our assessment that this would only affect a small number of stakeholders? If you disagree, please provide further evidence or examples of the wider impact this has on prospective listing applicants and proposed amendments.

No. The Panels do not agree that the existing requirements affect only a small number of issuers. In their experience, the track record requirements have caused significant additional work in a large number of both actual and also aborted premium segment IPOs and do not on many occasions result in helpful disclosure for investors.

For many prospective issuers, determining whether the financial information that has already been published or will be published in the prospectus will satisfy the eligibility requirement is not straightforward and the issuer and its advisers may need to discuss the issue with the FCA. This is particularly the case where the issuer has entered into one or more acquisitions in the three year period before listing whose size in aggregate is close

to the 25% threshold, where applying one or more of the ratios used to assess the size of the acquisition(s) could produce an anomalous result, or where the value of the business or asset acquired has changed significantly since it was acquired. The process outlined above can deter and has deterred prospective issuers from listing on the premium segment or in London at all, particularly in the cases where the issuer is considering alternative listing venues that do not impose such an eligibility requirement. In addition, where a company has grown acquisitively, its track record may well reflect a different business model that may not be of much relevance to the current operations of the business.

There is a significant amount of work and cost involved in the preparation of the financial information and whilst it is paramount that the financial track record is useful to investors and representative of the new applicant, as an example of historic performance and more importantly as an indicator of future performance, there are instances where the rules and their application are such that financial information presented is not necessarily representative and merely adds length and confusion to prospectuses.

It is possible that the many circumstances where the track record requirements being an impediment to new applicants have not been discussed with the FCA, given the advisers' collective experience of formerly new applicants needing to provide financial information for a single site, or a business which has been fully amalgamated into the 'at IPO' group. This may, for example, involve a business bought from receivership or where a company which is substantially assets experiences significant changes to historic assets or operational costs, meaning that the historic financial information is not representative of the business. There may be as little as one day of track record missing because of the historic completion process or ownership for the 'common control' analysis and as such these potential new applicants would have been advised that there is no certainty.

Companies may be discouraged because of historical precedent, namely by examples of new applicants who went through the eligibility process, spent money on creating a financial track record, only to find later in the review process that they were not eligible. There is significant cost and effort involved in creating a financial track record for a business under group IFRS, particularly one that is fully consolidated and historically might have produced accounts in UK or other GAAP, over and above the IPO process or listing process itself and as Boards needed to continue to run the business. The alternative, for which the FCA may not always accept the rationale, of directors stating that preparation of accounts is 'impossible' is by its nature problematic for Boards especially where an undertaking that it financial information is not representative might be more palatable and could be supported by the accountants or auditors.

Investors are sufficiently protected by the prospectus requirements which, as set out in the CP, include requirements in respect of:

- (i) three years of audited financial statements;
- (ii) where the issuer has a 'complex financial history' or has made a 'significant financial commitment', financial statements relating to any entity that the issuer has acquired; and
- (iii) additional information investors need to make an informed assessment.

If the FCA does not consider it appropriate to remove the track record requirements, it should approach the requirements in a more flexible and holistic way and publish guidance on when it may be prepared to waive the requirements.

Alternatively, an approach could be adopted whereby an issuer that does not have a complete track record should have to disclose that fact together with the reasons why as well as the potential risks that an investor may be exposed to as a result. Investors would then be able to make their own assessment of the situation and ask for more information if they felt they needed it or, in extreme scenarios, decide not to invest.

In any event, the FCA should not wait until it conducts a wider review of the prospectus regime following the current HMT consultation in order to reconsider the track record requirements.

Q28: What types of companies struggle to meet the existing requirement in the premium segment for a 3-year revenue track record covering 75% of the business? What alternatives could be considered for these companies?

Examples of companies that may struggle to meet the existing requirement include:

- Companies that are acquisitive. This may be particularly relevant to companies in the tech/fintech, pharma/biotech or media sectors, though companies in all sectors can be acquisitive.
- Companies owned by private equity firms that are pursuing a 'roll-up' strategy – i.e. a strategy of investing in one company in a sector and then acquiring others including those companies having been historically acquisitive, typically over a period of months or a few years, to create a combined entity with more commercial weight, which is then sold or floated.
- Companies that are not property or mineral companies but that either have a lot of joint ventures at the time of listing - for example, where significant parts of their business are located in countries whose local law requires a majority stake to be locally-owned - or that have recently bought out their joint venture partners.
- Companies consisting of various discrete businesses or entities that have been combined together so they can be spun out of a group.
- Companies that were historically substantively or entirely part of a larger corporate and subsequently acquired, where levels of materiality for the standalone business differ from the new applicant structure.

In addition, the same issues potentially arise on a reverse takeover where the listed company seeks to have the shares in the combined entity re-admitted to the premium segment (LR 5.6.21). In such circumstances, it is necessary to assess whether financial information has been published that covers 75% of the combined entity and where there is a 'look-through' on a Class 1 acquisition in LR13.5.1 and a similar concept applies.

Q29: Do you foresee any unintended consequences of these changes intended to modernise the Listing Rules, Disclosure Guidance and Transparency Rules and the Prospectus Regulation Rules?

Nothing that the Panels would want to flag at this stage.

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