Financial Conduct Authority

Consultation Paper CP17/5**

Reforming the availability of information in the UK equity IPO process

March 2017

Contents

We are asking for comments on this Consultation Paper by 1 June 2017

You can send them to us using the form on our website at:
www.fca.org.uk/cp17-05-response-form.

Or in writing to:

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We have developed the policy in this Consultation Paper in the context of the existing UK and EU regulatory framework. We will keep the proposals under review to assess whether any amendments will be required due to changes in the UK regulatory framework, including as a result of any negotiations following the UK's vote to leave the EU.

We make all responses to formal consultation available for public inspection unless the respondent requests otherwise. We will not regard a standard confidentiality statement in an email message as a request for non-disclosure.

Despite this, we may be asked to disclose a confidential response under the Freedom of Information Act 2000. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by the Information Commissioner and the Information Rights Tribunal.

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Abbreviations used in this paper

CBA	Cost benefit analysis
COBS	Conduct of Business sourcebook
CP	Consultation Paper
DP	Discussion Paper
ECM	Equity Capital Markets
ESMA	European Securities and Markets Authority
FCA	Financial Conduct Authority
FSA	Financial Services Authority
FSMA	Financial Services and Markets Act 2000
IPO	initial public offering
ITF	intention to float
MAR	Market Abuse Regulation
MiFID	Markets in Financial Instrument Directive
MTF	multilateral trading facility
SME	small and medium sized enterprise
UKLA	United Kingdom Listing Authority

1. Overview

Introduction

1.1 The initial public offering (IPO) process plays a vital role in helping companies raise capital in the UK's markets. Having gathered evidence as part of the market study into investment and corporate banking[1], our Discussion Paper (DP) on the availability of information in the UK equity IPO process (DP16/3)[2] identified some areas of the current process that called for improvement, namely the timing, sequencing and quality of information being provided to market participants.

1.2 The prospectus, which should be the primary source of information on the issuer, is currently made available late in the process. Arguably, investors do not have access to this key document sufficiently early for it to play its proper role in informing their investment decisions. Rather, investor education and initial price discovery are driven by 'connected' research produced by analysts within banks that are part of the IPO's book-running syndicate providing underwriting or placing services to the issuer (syndicate banks). Moreover, analysts within non-syndicate banks and independent research providers lack access to the information they need to produce 'unconnected' research on an offering. A number of recent external reports[3] raised this concern prior to the publication of DP16/3, but so far there have been no changes in market practice. This suggests that a policy intervention is necessary to facilitate reform.

1.3 Evidence reported in DP16/3 and the market study also highlighted how analysts from prospective syndicate banks are often involved in meetings with the issuer's management and their corporate finance advisers, prior to the formation of an underwriting syndicate. This heightens the risk of bias being imparted to their research.

1.4 Feedback from stakeholders on DP16/3 provides strong support for reforming the availability and quality of information in the UK IPO process, with a general recognition that such reforms would further enhance the effectiveness of the UK's primary equity markets as a place for raising capital. In addition, stakeholders have provided evidence highlighting further conduct risks associated with the production of connected research.

1.5 The structure of this Consultation Paper (CP) is as follows:

- Chapter 2 summarises stakeholder feedback on DP16/3.

1 MS15/1.2: Investment and corporate banking market study: Interim report (April 2016)

2 DP16/3 'Availability of information in the UK equity IPO process' (April 2016).

3 See Association of British Insurers, Encouraging Equity Investment (July 2013); An Independent Review for the Secretary of State for Business, Innovation & Skills: IPOs and Bookbuilding in Future HM Government Primary Share Disposals (December 2014); TheCityUK, Capital Markets for Growing Companies: A Review of the European Listings Regime (July 2015; The Investment Association, Supporting UK Productivity with Long-Term Investment: The Investment Association's Productivity Action Plan (March 2016).

- Chapter 3 identifies and assesses the key points of contention raised through the feedback.
- Chapter 4 proposes a package of policy measures to address identified concerns and improve the IPO process in the interest of issuers and investors. These proposals build upon some of the earlier ideas considered in DP16/3.
- Chapter 5 then considers whether it is appropriate to apply the proposals to IPOs on MTFs, notably the AIM and NEX Exchange growth markets.

Concerns with the UK IPO process

1.6 DP16/3 reported evidence on a typical timetable for an institutional-only IPO[4] in the UK and the way information on the issuer is made available to market participants. We found that, during what is characterised as the 'private phase' of an IPO transaction, prior to an intention to float (ITF) announcement, an 'analyst presentation' is organised, where the issuer's management presents information on the company to 'connected' analysts within the syndicate banks to support the preparation of their connected research. This analyst presentation typically takes place around four weeks ahead of the ITF announcement.

1.7 At the time of the ITF announcement, standard practice is for connected analysts to publish connected research and for the syndicate to then impose a 'blackout' period of 14 days. During this period, connected analysts use their research to provide select institutional investors with their views on the issuer, in a process known as 'investor education'. This investor education period is used to determine the initial price range within which the offer price is expected to be set, which is then circulated to certain institutional investors alongside a draft price range prospectus (the so-called 'pathfinder' prospectus). The pathfinder is shared with potential institutional investors to assess the anticipated level of demand for the offer before a further 14-day period of active marketing, known as the management roadshow, during which book-building takes place. At the close of this period the final approved prospectus is then typically published with an agreed offer price and size of the offer, followed by the relevant securities being admitted to trading.

1.8 The pathfinder is, therefore, made available relatively late in the process and only to a select group of potential institutional investors. The final approved prospectus itself becomes publicly available only once the offer has effectively closed. Coupled with a lack of access to the issuer's management, this also means that unconnected analysts generally lack access to the necessary information (unless the pathfinder is shared with them by a target investor) from which they would produce IPO research on similar terms to connected analysts. As a result, connected research is generally the only source of information available to investors during a crucial phase of investor education and initial price discovery.

1.9 DP16/3 and the final report of the market study[5] also highlighted some wider conduct risks associated with the production of connected research. It is common practice for analysts within prospective syndicate banks to meet the issuer's management and their corporate finance advisers prior to an underwriting or placing mandate being awarded, alongside investment banking pitching efforts. We found that corporate finance advisers typically ask questions of analysts about their views of the sector and its prospects, and that advisers consider a positive research message conveyed by analysts as being one of the main factors when advising the issuer on which

4 An 'IPO' in the UK is typically to only institutional investors.

5 See paragraphs 3.72 to 3.74 of MS15/1.3: Investment and corporate banking market study – final report (October 2016).

banks to appoint to the syndicate. The nature of this engagement heightens the risk of bias being imparted to connected research, noting here the 2014 enforcement case in the US surrounding the Toys 'R' Us IPO in 2010, where ten US broker dealers were found to have used their equity research analysts to win investment banking business by offering favourable research coverage[6] .

1.10 Through feedback received on DP16/3, we have uncovered some further evidence on the production of connected research, which points to conduct risks at all key stages of the IPO process. We have heard views from various stakeholders suggesting that:

- Corporate finance advisers place significant pressure on analysts to produce favourable research coverage if their bank is to secure a place on the syndicate.
- Even once an underwriting mandate has been accepted, favourability of research can be used to determine a bank's position in the syndicate.
- Review processes put in place for connected research by the issuer's advisers create pressure for analysts across the syndicate to publish a single common view, common forecasts and to control messaging through connected research during investor education and price formation.

1.11 It is the responsibility of investment banks to ensure that they manage any conflicts of interest in the production and dissemination of connected research. This includes ensuring that analysts do not come under any pressure to produce favourable research on an offering as a result of commercial incentives (including within the firm itself).

1.12 The concerns raised above about current market practice in relation to the IPO process create risks to our operational objectives:

- Market integrity is jeopardised if investors and issuers lose confidence in the UK IPO market because price formation is based on connected research, which is potentially biased or perceived as biased, rather than on information in an approved prospectus.
- Consumer protection is weakened when prospective investors cannot obtain timely access to the information they require and are instead forced to rely on connected research that is potentially biased or perceived as biased.
- Effective competition is inhibited because unconnected analysts face barriers to produce IPO research, which prevents competitive dynamics from enhancing the quality of connected research, and which prevents investors from accessing competing views on the offering and the issuer's prospects.

1.13 In addition, on the basis of initial evidence we have gathered, we have identified some practices that are potentially inconsistent with the Market Abuse Regulation (MAR) in the context of the disclosure of information to market participants during a typical IPO process. We would like to explore these further with market participants through this consultation process.

6 https://www.finra.org/newsroom/2014/finra-fines-10-firms-total-435-million

Policy options outlined in DP16/3

1.14 To address these issues, in DP16/3 we identified the need for a policy intervention aimed at:

- restoring the centrality of an approved prospectus document in the IPO process,
- enhancing standards of conduct throughout the process, in particular in the management of the inherent conflicts of interest in the production and distribution of connected research, and
- creating the necessary conditions for unconnected IPO research to be produced.

1.15 To stimulate debate, DP16/3 suggested three possible models for a reformed IPO process, which can be summarised as follows:

- **Model 1:** requiring a blackout on connected research until seven days after an approved prospectus or registration document is published,
- **Model 2:** opening any analyst presentation to unconnected analysts and requiring a blackout on connected research until seven days after the publication of an approved prospectus or registration document, and
- **Model 3:** opening any analyst presentation to unconnected analysts and prohibiting such a meeting from taking place before the publication of an approved prospectus or registration document.

Summary of our proposals in this Consultation Paper

1.16 Feedback on DP16/3, obtained through formal responses from stakeholders and a detailed programme of stakeholder engagement, suggests widespread support across market participants for the three aims set out in that paper and above. Whilst there is widespread support for the earlier publication of an approved prospectus or registration document, there are diverging views on one aspect of the reforms envisaged in DP16/3, namely whether the FCA should mandate temporal separation between the publication of an approved prospectus or registration document and connected research. There are also more nuanced views on the terms and timing of any management access for unconnected analysts.

1.17 This CP, therefore, proposes a package of policy measures which build on the earlier ideas considered in DP16/3 to address our concerns with the process, but which seek to balance the views of a range of market participants. There are two core components to our policy proposals.

1.18 The first measure is a series of new Handbook rules which seek to ensure that an approved prospectus or registration document is published, and unconnected analysts have access to the issuer's management, before any connected research is released. This is intended to restore the primacy of an approved prospectus document, significantly improve the range and quality of information available to investors, and facilitate the availability of such information early enough in the process to support more balanced investor education and price discovery.

1.19 The proposed rules should also allow issuers and syndicate banks to retain flexibility over how best to conduct transactions on a case-by-case basis. If unconnected analysts are provided

with an opportunity to access management on equal terms to connected analysts, the rules would allow connected research to be released from one day after an approved prospectus or registration document is published. If, however, issuers had a preference to communicate with unconnected analysts at a later stage than connected analysts, they could do so provided that connected research is not released until at least seven days after an approved prospectus or registration document is published. This would help to provide unconnected analysts with a chance to prepare research in time for when connected research is released and investor education and price discovery commences.

1.20 The second measure is new Handbook guidance clarifying our expectations on analysts' interactions with the issuer's management and their corporate finance advisers around the time an underwriting or placing mandate and subsequent syndicate positioning is being considered. We propose supplementing our existing guidance in COBS 12.2.9G[7] to clarify that we would regard any interaction between analysts and issuers or their representatives to be participation in investment banking pitching efforts until: (i) the firm has accepted a mandate to carry out underwriting or placing services for the issuer; and (ii) the firm's position in the syndicate has been determined.

1.21 The new guidance is intended to mitigate the risk of bias being imparted to connected research, thereby reinforcing the benefits brought about through the rule change.

Who does this consultation affect?

1.22 The proposals in this CP will affect investment banks providing both underwriting and placing and research services, issuers, investors, independent research providers, corporate finance advisers, and operators of regulated markets and multilateral trading facilities (MTFs).

Is this of interest to consumers?

1.23 The proposals in this CP will be of direct interest to institutional investors participating in an initial offering of equity shares. They will also be relevant to individual retail investors directly participating in an initial offering of equity shares, or whose funds are being invested through institutional investors (e.g. through a pension fund).

Equality and diversity considerations

1.24 We have considered the equality and diversity issues that may arise from the proposals in this CP. Overall, we do not consider that these adversely impact any of the groups with protected characteristics i.e. age, disability, sex, marriage or civil partnership, pregnancy and maternity, race, religion and belief, sexual orientation and gender reassignment.

1.25 We will continue to consider the equality and diversity implications of the proposals during the consultation period, and will revisit them when publishing the final rules. We welcome any input to this consultation on such matters.

7 Note that, as part of our consultation on the domestic implementation of MiFID II, we are proposing to change the numbering of provisions in COBS 12 (see Appendix 1 of CP16/29: Markets in Financial Instruments Directive II Implementation – Consultation Paper III). This will be relevant to other references to existing COBS 12 provisions throughout this CP.

Next steps

1.26 Please send us your comments on this CP by 1 June. To submit a response, please use the online response form on our website or write to us at the address on page 2.

1.27 After the consultation period has closed, we will consider stakeholder feedback. Depending on the nature of feedback, we would expect to publish a Policy Statement outlining any Handbook changes later in 2017.

2. Feedback on DP16/3

2.1 In this chapter, we summarise the feedback received on DP16/3. We received 36 written responses. Significant feedback was also gathered through bilateral meetings held with a range of market participants including investment banks, institutional investors, law firms, corporate finance advisers, private equity houses and various trade associations. Many of these stakeholders did not respond individually, but contributed to responses from relevant trade associations.

2.2 This chapter is purely descriptive. We will provide an analysis of this stakeholder feedback in subsequent chapters.

2.3 We have identified the following five key themes which emerged from stakeholder feedback on DP16/3:

- timing of prospectus publication
- conduct of analysts in the production of connected research
- the role of connected research
- the role of unconnected research
- 'blackout' periods, and
- application of reforms to IPOs on MTFs.

Timing of prospectus publication

2.4 A clear majority of respondents agreed that reform was required to restore the centrality of a prospectus document. There was widespread support, including from investment banks, for the earlier publication of at least an approved registration document (i.e. information relating to the issuer). The corporate finance advisory community also indicated that it would support this change, though these firms emphasised that we should be mindful of the possibility of this reform resulting in a longer IPO timetable.

2.5 Feedback from buy-side investors indicated strong support for an early publication of an approved prospectus or registration document. Emphasis was placed on the prospectus being the main source of information they require before making an investment decision, and that this would be of greatest use if it were made available by the start of the public phase of the process. Buy-side firms told us that this would allow them to have much longer with an official disclosure document, giving them more time to build robust financial models to analyse the company's prospects and reach an investment decision.

2.6 Independent research providers supported earlier publication of an approved prospectus or registration document. These firms have said that this would be a significant improvement on

current practice, removing one of the barriers preventing them from being able to produce IPO research. However, their feedback suggests that access to management is also essential as this would allow them to ask questions about the company and to understand the nuances of management's views, therefore, placing them on a more level playing field with connected analysts.

2.7 A representative of small and medium-sized enterprises (SMEs) has said that, whilst earlier publication of an approved prospectus document is welcome, the FCA should be mindful of any additional costs that might be created for SMEs, particularly if the market moves towards a model whereby an early prospectus is then supplemented by an additional document later in the process.

Conduct of analysts in the production of connected research

2.8 A number of responses from the investment banking, legal and corporate finance advisory communities confirmed our view that corporate finance advisers are indeed placing significant pressure on analysts to provide views on company valuation and to produce favourable research coverage if their bank is to secure a place on the book-running syndicate. Despite the protocols that corporate finance advisers have in place on their interactions with analysts at investment banks[8], feedback from one large corporate finance advisory firm made it clear that, in addition to using these meetings to understand an individual analyst's capability and knowledge of the sector, they like to gain comfort that the analyst would write positive research on the issuer. We were told that advisers want the analyst to use their expertise to 'sell' the company, and that analysts could not be relied on to do so if they were likely to produce research that was not positive. The firm told us that this was the main factor they consider when advising an issuer on which banks to appoint to the syndicate.

2.9 Both Equity Capital Markets (ECM) and research staff within some investment banks have suggested that this type of pressure makes it very difficult for both the firm and its analysts to manage their conflicts of interest. The research division of a major bank told us that they would be more comfortable if these meetings did not take place, provided there was a level playing field (i.e. analysts from other banks also did not have these meetings). On the other hand, staff within some research divisions have suggested that these meetings can be helpful in understanding the company and that early engagement supports high quality research. Some have suggested that involvement at this early stage of the process allows them to form their own views on attractiveness of the potential IPO and to steer their investment banking colleagues away from participation in IPOs where the balance of advantage would suggest non-participation.

2.10 One law firm also explicitly expressed concerns that the systems and controls within investment banks designed to manage conflicts of interest in the production of connected research are coming under increasing strain as a result of the commercial pressures stemming from the issuer and its advisers, and from within the firm itself, to produce positive research on the issuer during IPOs.

2.11 We heard views within the investment banking community that, even once an underwriting or placing mandate has been accepted, corporate finance advisers tend to rely on the favourability of research to inform the advice they give to the issuer when determining a bank's position in the syndicate.

2.12 Some banks have also suggested that the review processes put in place for connected research by the issuer's advisers creates pressure on analysts across the syndicate to publish a single

8 See paragraph 3.73 in the final report of the market study of investment and corporate banking.

common view, common forecasts and to control messaging through connected research during investor education and price formation.

The role of connected research

2.13 In DP16/3, we gave consideration to whether connected research should continue to be a feature of the IPO process, given the conduct concerns with the way it is produced. We considered the implications of a process where marketing and book-building is conducted using only an approved prospectus or registration document, as is the case under the US regulatory framework. However, since our feedback at the time suggested that buy-side firms saw some value in connected research, the reform models outlined in DP16/3 all assumed that it played a continued role.

2.14 Investment banks have said in their feedback that connected research plays a valuable role in the IPO process. We were told by staff within both ECM and research divisions of banks that the early involvement of connected analysts places them in a strong position to produce insightful pieces of analysis on the company. In particular, access to the issuer's management provides helpful interpretative colour on the company information contained within the prospectus, including financial forecasts of key performance indicators. Banks have said that these insights play a valuable role in price discovery through a two-week period of investor education which currently follows the ITF announcement and the circulation of connected research. These views are also held by a representative of SMEs and a market operator.

2.15 Feedback from buy-side investors was more varied and nuanced on the importance of connected research. Several firms have said that they would want to see a continued role for connected research, valuing its brevity compared with the prospectus, and the forecasts of key company financial information. Others, however, told us that connected research is not a crucial feature of the process and the existing sequencing of connected research and the pathfinder prospectus does not result in optimal price formation.

The role of unconnected research

2.16 In DP16/3, we reported evidence suggesting that unconnected research on IPOs is extremely rare. We found that, between January 2010 and May 2015, unconnected research was published during the IPO process on only one of the UK's 169 IPO transactions. We found that there were two main barriers to the production of unconnected research: (i) the late availability of the approved prospectus, which is typically published following book-building and on the first day of trading; and (ii) lack of access for unconnected analysts to the issuer's management.

2.17 We said that this lack of unconnected research was particularly problematic given the concerns about connected research being subject to bias, and that this was the only source of information available to investors during investor education and initial price discovery. We suggested that an avenue for reform could be to open up the analyst presentation so that unconnected analysts can meet the issuer's management alongside connected analysts. This policy measure, if introduced alongside a measure to bring about earlier prospectus publication, would help to create the necessary conditions for unconnected analysts to produce IPO research and act as mitigant to the perceived bias in connected research by introducing competing and more varied views on the prospects of the issuer.

2.18 There are two aspects of the feedback on DP16/3 relating to the role of unconnected research in the IPO process: (i) questions around the demand for unconnected IPO research; and (ii) the terms of management access for unconnected analysts.

Demand for unconnected IPO research

2.19 Investment banks have expressed scepticism over whether a market for unconnected IPO research would emerge, with some arguing that there is no concrete evidence to suggest that there would be any demand for it. Some banks have referenced attempts to foster more unconnected research in other jurisdictions, but with limited success. A number of banks recognise that, if there is demand for unconnected research, then the emergence of an additional source of information would support investor decision-making.

2.20 Feedback from buy-side investors was unanimous in supporting our aim to create the necessary conditions for unconnected research to feature in the IPO process. A number of buy-side firms have said that they would like to see more unconnected research available during the IPO process, and they would be willing to pay for it, particularly on larger transactions. These firms told us that they would value an alternative opinion on a transaction. Some buy-side firms told us that, where unconnected research has been produced in the past, they have paid for it either through an existing subscription service (i.e. within the existing retainer they are charged by the research provider) or as a bespoke piece of analysis. Independent research providers told us that they are frequently approached by existing or new buy-side clients with requests for analysis on an offering, but they are almost always unable to satisfy that demand due to the lack of access to available information on the issuer.

Management access for unconnected analysts

2.21 Whilst all respondents acknowledge that publication of an earlier approved prospectus or registration document would support the conditions required for unconnected research to feature in the IPO process, the investment banking and legal communities expressed concern over how and when any management access for unconnected research would be given. The general view across these groups was that any unconnected analyst meeting should not be mandatory and should be at the issuer's discretion on a transaction-by-transaction basis. In particular, they said they would have concerns with unconnected analysts having access to the issuer's management alongside connected analysts, which typically takes place in the private phase at an analyst presentation around four weeks before the ITF announcement. Banks expressed concerns that, at this meeting, unconnected analysts would be exposed to information which could create subsequent execution risk for the issuer. Given these concerns, these firms have a strong preference that any mandatory access of management should, if at all, be offered after the publication of an approved prospectus or registration document.

2.22 Some banks and law firms told us that, even if unconnected analysts were provided with an opportunity to meet the issuer's management after the approved prospectus or registration document were published, legal liability risks would arise through the possibility that unconnected analysts distribute their research into other jurisdictions outside of the UK, notably the US. We were told that research may be incompatible with securities law in these other jurisdictions, which may attach liability to the issuer or advisers involved in the offering. Some banks and law firms have said that, to manage any such liability risk, unconnected analysts would need to adhere to research guidelines which, among other things, govern the distribution of research.

2.23 Feedback from independent research providers emphasised that they would require access to the issuer's management as early in the process as possible, and that this is essential to enable them to produce insightful research. As noted above, these firms have stressed the importance of meeting the issuer's management alongside connected analysts to ensure that all IPO research is produced on a level playing field. Many of these firms have also said that this management access would be beneficial if provided after the publication of a prospectus or registration document, to allow them to digest company information. This suggests an IPO process similar to 'Model 3' in DP16/3, whereby both connected and unconnected analysts meet management in the public phase of the process. Some firms said that, ideally, they would

require seven days with the prospectus or registration document to allow them to digest company information so that they can ask constructive questions at the management meeting.

2.24 Buy-side investors have said that, to give unconnected analysts as much time as possible to produce their research in time for the ITF announcement (i.e. when investors want it), they should be given an opportunity to access the issuer's management alongside connected analysts. The clear message delivered by buy-side firms is that the latest point they would need to receive unconnected research for it to be useful is at the start of the management roadshow and book-build. Ideally it would come earlier to support investor education and initial price discovery.

Blackout periods

Drivers of existing blackout period

2.25 Through DP16/3, we wanted to gain a better understanding of the drivers of the existing blackout period, specifically the delay between the release of connected research and the prospectus documentation. We were aware that investment banks typically attributed this to management of both legal liability and regulatory risk, but we wanted to understand precisely where these risks stemmed from.

2.26 Feedback from the legal and investment banking communities outlined the perceived legal liability risks that drive the existing blackout period. We were told that there is perceived to be material potential liability risk to issuers from any inaccuracies in connected research which could be regarded as part of the issuer's offering materials if the prospectus and research are released close together. That is, an investor may seek to claim that their investment decision relied on a disclosure in connected research, which subsequently turned out to be untrue, inaccurate, or misleading. We were told that such a claim could potentially be brought against the firm producing connected research, including for breach of contract, misrepresentation or negligent misstatement, and against the issuer on the basis that the connected research was produced under its authority or with its approval.

2.27 The general view from within the legal and investment banking communities appears to be that, in the absence of any temporal separation between the release of connected research and the subsequent prospectus, investor education (currently conducted using connected research) and the management roadshow and book-build (currently conducted using a pathfinder prospectus) may become less distinct activities, therefore, increasing the perceived risk that an investor may claim to have relied on connected research rather than the prospectus when making an investment decision.

2.28 In terms of management of regulatory risk as a driver of the existing blackout period, investment banks had previously suggested that the existing COBS 12.2.12G[9] was relevant here. However, in DP16/3, we made clear that this Handbook provision should not drive the existing blackout period because: (i) the existing market practice of a blackout period pre-dates COBS 12.2.12G, which was the outcome of an FSA consultation in 2003[10]; (ii) the FSA's original proposal in 2003 was to introduce a Handbook rule requiring syndicate banks to impose a 'quiet period' on connected research of 30 days after the publication of the prospectus, which is different from the existing pre-prospectus blackout period[11]; and (iii) when, as part of our information request for the investment and corporate banking market

9 COBS 12.2.12G states that a firm should consider whether its conflicts of interest policy should contain restrictions on the timing of the publication of investment research, given other activities of the firm which could create the perception that investment research may not be impartial, e.g. restricting the publication of investment research around the time of an offering.

10 CP171 and CP205, see http://www.fsa.gov.uk/pubs/cp/cp205.pdf

11 Although the FSA did not prescribe a precise post-prospectus quiet period, the outcome of the consultation was to introduce the guidance currently in COBS 12.2.12G.

study, we asked banks how they ensure research is objective, none actually gave COBS 12.2.12G compliance as their means of achieving this.

2.29 In their feedback on DP16/3, few investment banks continued to place emphasis on COBS 12.2.12G as the driver of the existing blackout period. In fact, one smaller bank explicitly agreed with our comments in DP16/3 that the COBS provision does not drive the blackout. However, some respondents from within the legal community have suggested that the blackout period is considered as an important conflicts management tool through demonstrating the independence of analysts' activities (e.g. producing research and conducting investor education) from ECM activities (e.g. roadshow and book-building).

2.30 Some stakeholders from the legal community also referenced UKLA Technical Note 604.1, which refers to the use of blackout periods as one factor that firms should consider when determining whether research falls within the definition of an 'advertisement' under Prospectus Rule 3.3.2.R.

Concept of mandatory blackout periods in a reformed IPO process

2.31 Whilst the earlier publication of an approved prospectus or registration document is widely acknowledged to be an improvement to current market practice, a number of stakeholders from across the market questioned whether the FCA should mandate a blackout period following the publication of an approved prospectus or registration document and before any connected research can be released. A central idea in two models outlined in DP16/3 was for banks to impose seven days of separation between the two documents. This was intended to: (i) restore the primacy of an approved prospectus document by isolating it as the only source of information for the first seven days of the process; (ii) mitigate any conduct risks associated with the production of connected research; and (iii) provide unconnected analysts with key information required to produce IPO research.

2.32 Feedback suggests that the majority of buy-side firms would prefer that all information on the IPO (i.e. a prospectus or registration document, along with connected research and unconnected research) was released simultaneously at the beginning of the public phase of the process. Most buy-side firms regard any form of blackout period as unnecessarily lengthening the IPO timetable. Some buy-side firms said that, if connected research was published alongside a prospectus, they would look at research first to form an initial view, before turning to the prospectus for further detail. A representative of SMEs also said that a simultaneous publication of the prospectus and connected research should be the desired objective for reform.

2.33 Respondents from the investment banking and legal communities told us that simultaneous publication of a prospectus or registration document and connected research is unlikely to be deliverable. Investment banks have said that they are comfortable with the idea that connected research should follow a registration document but, to manage legal liability risks, they would impose temporal separation between the two documents. Representatives of the large investment banks indicated that a registration document could be published in the private phase of the process, up to seven days ahead of the ITF announcement and connected research, with a final integrated prospectus containing the price range of the issue being published two weeks later at the end of the investor education period and the beginning of the management roadshow and book-building. They said that the publication of a registration document ahead of the ITF announcement would be intended to avoid any lengthening of the IPO timetable and minimise any additional execution risk. However, the investment banking community suggested that the FCA does not need to mandate a blackout period after publication of the prospectus or registration document, and that issuers and banks should retain flexibility to assess the appropriate length on a transaction-by-transaction basis.

2.34 Feedback from independent research providers and investors is clear that unconnected analysts should be given the same opportunity as connected analysts to produce IPO research. Some firms indicated that a blackout period following the publication of a prospectus document would be desirable to the extent that unconnected analysts have not had access to the issuer's management alongside connected analysts. Under these circumstances, connected analysts may have had a much longer lead time to analyse and digest information and produce research. Other independent research providers have indicated that, regardless of when they meet management, they would require at least seven days with the prospectus or registration document to ensure that they produce high quality research, implying that a blackout would be welcome.

Application of reforms to IPOs on MTFs

2.35 In DP16/3 we asked whether the types of reforms under consideration were likely to be appropriate for firms conducting IPOs on MTFs, notably the AIM and NEX Exchange growth markets. The majority of feedback from stakeholders did not differentiate between different types of market. However, a limited number of market participants told us that the ideas suggested in DP16/3 are unlikely to be appropriate in an MTF context. They argued that the dynamics in these markets means that the same types of market failure we have identified in a regulated market context would not exist for MTFs. We were also told that connected research can play a less prominent role than it does in offerings on regulated markets.

2.36 The same stakeholders suggested that, if the reforms under consideration resulted in improvements for IPOs onto regulated markets, they could envisage, as matter of market practice, an equivalent model being adopted for MTFs.

Additional evidence gathered on the UK IPO process

2.37 MAR requires controls on the flow of inside information. In this context, through some initial bilateral meetings with representatives across the legal community, as well as reviewing some material provided by some investment banks, we have looked at the type of information generated and shared in a typical IPO process.

Type of information shared throughout the UK IPO process

Early look meetings

2.38 We were told that, significantly in advance of taking any decision to undertake a transaction, prospective issuers considering an IPO typically hold 'early look' meetings with institutional investors. These are intended to inform investors on the company and gauge interest before a decision is made on whether an IPO is likely to be the most appropriate means of raising capital. We were told that the type of information that tends to be shared can vary, but is typically publicly available information on the company. This can be supplemented by an explanation of the various capital-raising options available to the company, or more specific detail on a possible upcoming IPO under consideration, e.g. timing and size of the transaction under consideration, the use of proceeds, and the current financial and operating performance of the company. In some cases where the possibility of an IPO is specifically addressed, these meetings may be preceded by a public announcement to make publically available any inside information that will be disclosed.

2.39 We were informed that the majority of these communications 'do not involve disclosures of inside information' and therefore that these meetings are usually conducted 'without making these individuals insiders'.

Analyst presentation

2.40 Based on initial feedback from some law firms and on our review of a selection of materials used at recent analyst presentations, it appears that the analyst presentation to connected

analysts, currently held three to four weeks before the ITF announcement, contains three broad types of information:

- Operational and financial information on the company, which typically includes an overview of the business, the structure of the company, its existing and/or planned board membership, and key financial and other indicators of performance.

- Details of the deal including the amount to be raised through the IPO, the relevant Exchange or other market or platform on which admission to trading is to be sought, the listing authority, and a projected timetable of key events for the transaction.

- Strategic and forward-looking information on the company which typically includes the business strategy and potential growth prospects.

Pilot fishing and anchor investor meetings

2.41 The initial evidence provided by some law firms also focused on 'pilot fishing' and 'anchor investor' meetings for prospective institutional investors. We were told that these take place before the ITF announcement (sometimes well in advance of the analyst presentation) though by this stage the issuer may already have indicated that an IPO is likely to happen. We understand that it is common for the issuer to share deal logistics with investors, as described above. We were told that issuers may also share specific information relating to the company's existing financial operating metrics, along with forward-looking information about its strategy and capital structure.

2.42 We were told that pilot fishing and anchor investor meetings are usually expected to be made on a 'wall-crossed' basis, with investors being 'made insiders'.

ITF announcement and subsequent events

2.43 We were told that an ITF announcement provides specific confirmation of the issuer's intention to carry out an IPO and may also make inside information public, and that the ITF announcement may constitute an announcement for the purposes of Article 11 of MAR. Based on a review of recent ITF announcements, information publicly disclosed to the market at this stage appears to include the same information contained within the analyst presentation, as described above.

2.44 The type of information shared following the ITF announcement, namely that shared during investor education and the management roadshow, was examined in DP16/3 and described in the overview chapter of this CP.

MAR considerations

2.45 Some law firms told us that, when an issuer already has listed debt or is a 'spin-off' from an existing listed company, they would be considered to fall within the definition of an 'issuer' as defined in Article 3(1)(21) of MAR, whereas first time issuers which will only come into the scope of the definition when they request admission to trading.

2.46 The legal community also recognise that, where the issuer falls within scope of MAR, careful consideration would need to be given to whether any of the information being disclosed during the IPO process constitutes inside information. However, it appears that market participants do not routinely consider whether disclosing information in the analyst presentation (to analysts and, in turn, the actual recipients of the analyst's research) is in accordance with Article 10(1) of MAR. In other words, they do not routinely assess whether the condition that disclosure has been made in 'the normal exercise of an employment, a profession or duties' is satisfied.

3. Policy analysis following stakeholder feedback on DP16/3

3.1 This chapter outlines the key policy questions arising from stakeholder feedback on DP16/3, which are analysed against our policy aims for reforming the UK IPO process.

Key policy questions to consider

3.2 As noted in Chapter 2, respondents expressed widespread support for the earlier publication of a prospectus or registration document. We have, however, identified three consequential policy questions about connected and unconnected research, which we have considered in determining a route forward. These are:

- Should connected research be permitted in the IPO process given the conflicts involved and our conduct concerns?
- If connected research should be allowed, should the FCA mandate temporal separation between the publication of an approved prospectus or registration document and connected research?
- What level of management access should be offered to unconnected analysts, and when and how should any access should be offered?

Should connected research be permitted?

3.3 The feedback from market participants on this aspect of DP16/3, as summarised in Chapter 2, calls into question the way that connected research is prepared, distributed and used to drive investor education and initial price discovery. In some cases, this feedback confirms many of the conduct risks identified in DP16/3, including around analysts' meetings with the issuer's management and their corporate finance advisers prior to an underwriting or placing mandate being awarded. However, the feedback also highlights further conduct risks not considered in DP16/3.

3.4 As recognised in DP16/3, meetings between analysts within prospective syndicate banks on the one hand, and the issuer's management and their corporate finance advisers on the other, creates a heightened risk of bias being imparted to connected research, particularly given that these meetings take place alongside investment banking pitching efforts.

3.5 It is the responsibility of investment banks to ensure that they manage conflicts of interest in the production and dissemination of connected research. This includes ensuring that analysts do not come under any pressure to produce favourable research on an offering around the time that an underwriting or placing mandate is being considered. Of particular relevance here is the existing COBS 12.2.9G which states that analysts should not become involved in corporate finance activity, including pitches for new business, and the existing COBS 12.2.5R(4) which prohibits firms from promising favourable research coverage. Despite what research staff within some investment banks have told us and the mitigation steps put in place by corporate

finance advisers, we have not been convinced that there are benefits of analyst involvement at this stage in the process which would outweigh the conflicts created and heightened risk that bias is imparted to connected research, and we consider the types of practices outlined above as being inconsistent with the existing COBS 12.2.9G.

3.6 A second conduct risk highlighted through feedback on DP16/3 relates to the way that research could be used to improve a bank's position in the syndicate. As raised in Chapter 2, we were told by one large investment bank that, even once an underwriting or placing mandate has been accepted, corporate finance advisers can link research content to the advice they give to the issuer when determining the role played by each bank within the syndicate. Again, it is the responsibility of investment banks to ensure that they manage conflicts of interest in the production and dissemination of connected research, including by ensuring that analysts do not come under any pressure to produce favourable research. This type of pressure further heightens the risk that bias is systematically imparted to connected research.

3.7 The third conduct risk we have identified through feedback from some investment banks relates to the fact that there appears to be very little variation in the forecasts contained within connected research produced by analysts from different banks across the syndicate. Feedback has suggested that this is due to the review processes put in place by the issuer's advisers as a way of controlling the messaging around the offering and driving price discovery. This suggests that the connected research is not independently prepared as required by COBS 12.2.

Q1: Are you aware of any other conduct risks associated with the production of connected research? If so, please describe them.

3.8 In the light of the significant conduct risks associated with the production of connected research, there is a question about whether this product should be permitted in the IPO process. Arguably, a prohibition on connected research could be considered appropriate if commercial interests (including from within the banks themselves) mean that banks are not effectively managing their conflicts of interest. The presence of the underlying conduct risks creates concerns in terms of investor protection and the integrity of price formation, given that investor education and initial price discovery is currently driven by connected research.

3.9 However, as acknowledged in Chapter 2, investment banks hold the view that connected research plays an important role in the process for educating investors and facilitating price discovery through a two-week period of investor education. In this context, some buy-side firms value the brevity of connected research compared to the prospectus, and the forecasts of key company financial information.

3.10 On balance, at this stage we do not favour a prohibition on connected research. Instead, any reform should focus on mitigating the conduct risks underpinning the production of research, including through more robust management of conflicts of interest. However, the FCA will continue to keep this under review. Moreover, as noted in the final report into investment and corporate banking, we will also continue to monitor the conduct of corporate finance advisers that are authorised firms.

Q2: Do you agree that connected research should continue to play a role in the UK IPO process?

Mandatory blackout period

3.11 The feedback reported in Chapter 2 suggests that, whilst there is widespread support for the earlier publication of an approved prospectus document, there are divergent views on whether

the FCA should mandate temporal separation between the publication of a prospectus document and connected research. Buy-side firms do not consider temporal separation as desirable. The investment banking community is likely to impose separation as a matter of practice, but would prefer the length not to be mandated. Independent research providers, however, see temporal seperation as justified, particularly if they have not had equal access to management to that provided for connected analysts.

3.12 In the absence of an explicit mandated period of separation between an approved prospectus or registration document and connected research, there is risk that the market moves towards simultaneous publication of these two documents. This outcome is inconsistent with our policy aims for the following reasons:

- **Reducing conduct risks:** If connected research is likely to continue playing too prominent a role in shaping investors' initial views on the company, and, therefore, in driving initial price discovery, this will not reduce the conduct risks underlying connected research outlined earlier and our associated concerns about investor protection and the integrity of price formation.

- **Centrality of the prospectus or registration document:** Whilst buy-side firms have said that they would like to see simultaneous publication of all information on an offering at the start of the process, several investors have told us that, if connected research is published alongside a prospectus, they would look at research first to form an initial view, before turning to the prospectus for further detail. This is because they value the brevity of connected research and the financial forecasts it contains. Particularly if there are risks that connected research is not wholly objective, it may be preferable to increase the relative prominence of the objectively-presented official offering document before the promulgation of connected research and any unconnected research.

- **It may not create the necessary conditions for unconnected research to emerge:** The simultaneous publication of an approved prospectus or registration document and connected research may act as a significant disincentive for unconnected analysts to produce research. By the time they would have seen the official offering document to begin digesting the company information and thinking about writing research, connected analysts would have already released their output, which will have begun to support investor education and initial price discovery. Several investors have said that for unconnected research to be most useful, it would need to be released in time for the two-week phase of investor education, and that the value of such research will significantly decline to the extent it is not available in advance of the management roadshow and book-build stage.

3.13 This analysis implies that sufficient temporal separation between a prospectus or registration document and connected research is necessary to advance our policy aims. The seven-day period suggested in DP16/3 could be appropriate on the grounds that unconnected analysts are likely to require at least this amount of time to produce high quality research. This seven-day period should, therefore, place them on a more level playing field with connected analysts. This would help to support more balanced investor education and price discovery that is not disproportionately driven by connected research.

Q3: Do you agree that simultaneous publication of an approved prospectus or registration document and connected research does not adequately address level playing field issues for unconnected analysts and still leaves connected research excessively prominent in initial price discovery?

Management access for unconnected analysts

3.14 The analysis above assumed that unconnected analysts are not offered any access to the issuer's management. However, this was a central component of the policy ideas suggested in DP16/3. Indeed, Chapter 2 has shown that stakeholders' views differ on the appropriate level of management access to be offered to unconnected analysts, and when and how such access should be offered.

3.15 The timing of access for unconnected analysts as compared with that for connected analysts would be important in determining the extent to which it might be possible that a mandatory seven days of separation between the publication of the approved prospectus or registration document and connected research could be reduced from the perspective of addressing our concerns with the process.

3.16 As outlined in Chapter 2, the investment banking community indicated its discomfort with the prospect of any communication between unconnected analysts and the issuer's management prior to the publication of an approved prospectus or registration document. These stakeholders were concerned that sharing information with unconnected analysts ahead of this point might create additional execution risk for the issuer. However, providing unconnected analysts with management access only at a later stage would place them at a disadvantage compared with connected analysts, who typically meet management through the analyst presentation around four weeks before the ITF announcement. This would, therefore, reinforce the importance of seven days of separation between the publication of an approved prospectus or registration document and connected research, to allow unconnected analysts sufficient time to prepare their research in time to support investor education and price discovery.

Q4: Do you agree that, if unconnected analysts were to be provided with access the issuer's management only at a later stage than connected analysts, there should be a mandatory seven-day period of separation before any connected research could be released?

4.
Policy proposals

4.1 In the light of the stakeholder feedback on the policy ideas suggested in DP16/3, together with our policy analysis of that feedback, in this chapter we outline our proposed package of policy measures for reforming the availability of information in the UK equity IPO process.

4.2 There are two core components to our proposals, which are considered, in turn, below.

Proposed Handbook rules

4.3 The first measure is a series of new Handbook rules which seek to ensure that an approved prospectus or registration document is published, and unconnected analysts have access to the issuer's management, before any connected research is released. This is intended to restore the primacy of an approved prospectus document, significantly improve the range and quality of information available to investors, and facilitate the availability of such information early enough in the process to support more balanced investor education and price discovery.

4.4 The proposed rules should also allow issuers and syndicate banks to retain flexibility over how best to conduct transactions on a case-by-case basis. If unconnected analysts are provided with an opportunity to be in communication with management on equal terms to connected analysts[12], the rules would allow connected research to be released from one day after a prospectus or registration document is published.

4.5 If, however, issuers had a preference to be in communication with unconnected analysts at a later stage than connected analysts, they could do so provided that: (i) the communication is substantially completed by the time connected research is released; and (ii) connected research is not released until at least seven days after an approved prospectus or registration document is published. This would help to provide unconnected analysts with a chance to prepare research in time for when connected research is released and investor education and price discovery commences.

4.6 Appendix 1 contains the proposed rules, which we intend to include in the new COBS chapter containing provisions governing underwriting and placing activity.

Q5: Do you agree that this proposed policy measure would effectively advance our objectives of enhancing market integrity, protecting investors and promoting effective competition? If not, how should it be amended? Please explain how your alternative suggestion would advance our objectives.

Q6: Do you agree with the proposed rules set out in Appendix 1? If not, how should they be amended?

12 Producers of IPO research are reminded that, at all times, including when attending meetings in the presence of other analysts, they should comply with competition law requirements, including in relation to the disclosure of confidential and/or commercially sensitive information.

4.7 Detailed feedback from the investment banking community has indicated that, to implement the type of reform envisaged in DP16/3, which is similar in substance to the proposed Handbook rules being considered here, an approved registration document could be published in the private phase of the process, up to seven days before the ITF announcement and connected research. They indicated that a single approved prospectus document, containing a price range, could then be published two weeks later at the end of investor education and the beginning of the management roadshow and book-building. We were told that this would prevent any lengthening of the IPO timetable and avoid any additional execution risk, noting that an approved registration document would not necessarily signal that a transaction is taking place in the way that an ITF announcement does.

4.8 The effective length of the IPO timetable is not expected to vary materially depending on when the issuer or syndicate banks choose to provide unconnected analysts with management access (i.e. alongside connected analysts or separately).

4.9 The model suggested by the investment banking community outlined above reflects some improvement to the current timing and sequencing of key information available throughout the process. However, when developing our proposals, we had envisaged the adoption of the 'tripartite' prospectus model allowed under EU prospectus legislation if the issuer had decided to begin on this route. In other words, where an approved registration document rather than a single approved prospectus is published before connected research is released, the issuer would then publish a securities note and summary document at a later stage of the process.

Q7: If you think that there are advantages to an alternative approach to the one we had envisaged, please provide details.

Q8: Does this proposal have any practical implications for the transaction review process?

4.10 Figures 1 and 2 below provide an indicative timetable of the IPO process which might result from the implementation of our proposed Handbook rules. These timetables are based on detailed feedback provided by the investment banking community.

Figure 1: Management access for unconnected analysts alongside connected analysts in private phase and a minimum one day separation between registration document and connected research

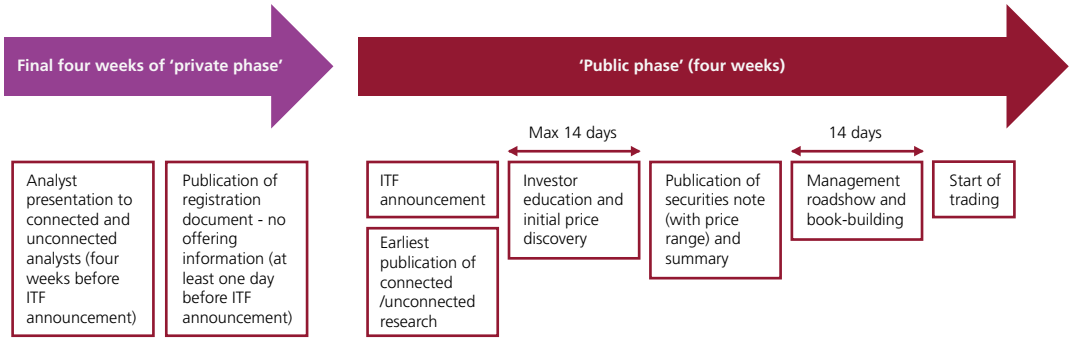
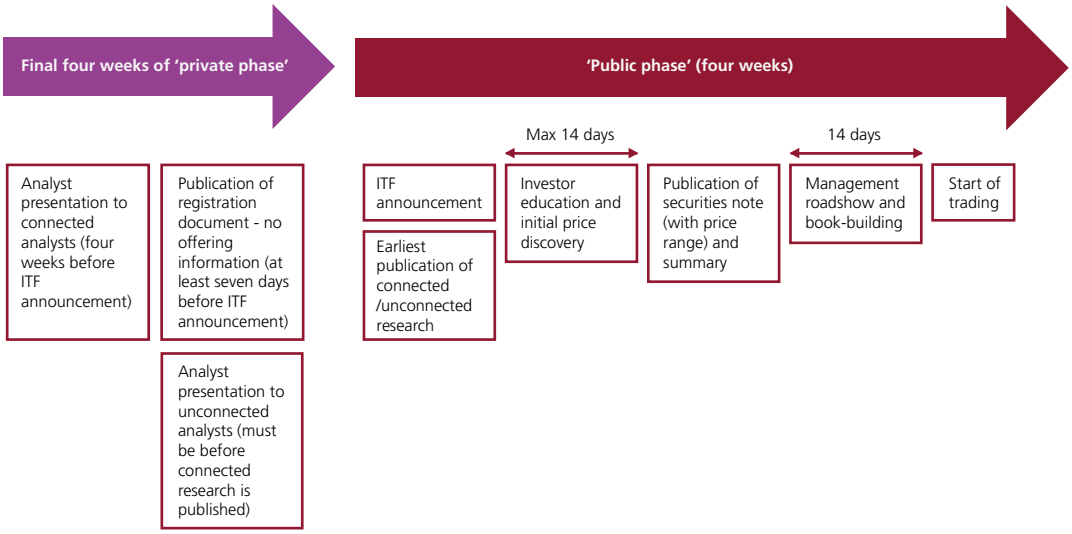


Figure 2: Management access for unconnected analysts post-registration document and seven-day separation between registration document and connected research



Practical considerations

4.11 Our proposed Handbook rules may raise some practical questions for syndicate banks around how unconnected analysts would be made aware of opportunities to be in communication with the issuer's management, and which analysts would be provided with such an opportunity. In addition, banks may have a legitimate interest in specifying the terms of access for unconnected analysts, particularly those aimed at preventing additional legal liability risk arising from any resulting unconnected research being distributed into other jurisdictions.

4.12 The proposed rules set out in Appendix 1 seek to deal with these issues in two ways. First, it requires syndicate banks to provide a 'range' of unconnected analysts with an opportunity to be in communication with the issuer's management, and specifies that the range must be one which, in the bank's opinion, creates a reasonable prospect of enabling investors to make a better-informed assessment of the issuer. Second, it specifies that the engagement of unconnected analysts must be on 'reasonable terms', recognising that geographical restrictions on the distribution of any resulting research would, in these circumstances, be deemed as 'reasonable'.

4.13 To help ensure that our proposal is operationalised in a way that balances the interests of all relevant market participants, we envisage working with trade associations representing investment banks and independent research providers to develop a form of common 'research guidelines' for unconnected analysts. The intention of these industry guidelines would be to specify the 'reasonable' terms of access and help determine what might be an appropriate 'range' of unconnected analysts to be offered management access. The relevant trade associations could then provide potential producers of unconnected research with an opportunity to sign up to these guidelines, with those that do so automatically being established as part of a community eligible to be in communication with the issuer's management on any equity IPO. This would prevent the need for syndicate banks to make an assessment on the terms of access and appropriate range for each individual transaction.

Q9: Do you think that the suggested industry guidelines would help to operationalise the proposed rule requiring syndicate banks to provide unconnected analysts with

an opportunity to be in communication with the issuer's management?

4.14 To the extent that syndicate banks choose to provide unconnected analysts with an opportunity to be in communication with the issuer's management separately from connected analysts, a further practical consideration is whether any web-based communication, conference call or email exchange between unconnected analysts and the issuer's management is appropriate, rather than physical meetings. This would be permitted under the proposed rule in Appendix 1. We welcome feedback on this from stakeholders as part of this consultation process, particularly whether or not the rule should require the opportunity of a physical meeting only.

Ensuring consistency with other relevant regulation

4.15 In Chapter 2, we reported some initial evidence we gathered on the disclosure of information to market participants during a typical IPO process and, in this context, the consideration being given to MAR by some law firms advising issuers. As part of the consultation process resulting from this CP, we would welcome further evidence from stakeholders on this, and specifically on how firms are justifying the disclosure of inside information in an analyst presentation as being in compliance with MAR.

4.16 We agree with stakeholders that have said that an issuer with debt securities admitted to trading on either a regulated market or a multilateral trading facility is within the scope of MAR. Subject to communication from the European Securities and Markets Authority (ESMA), we would broaden this to encompass any financial instrument admitted to trading or subject to a request for admission to trading on a relevant venue. We also agree that first time issuers will come into the scope of MAR when they make a request for admission to trading on a regulated market or MTF.

4.17 Article 10 and 14 of MAR respectively prohibit unlawful disclosure of inside information and insider dealing by any person. The handling of potential inside information is, therefore, of significant importance for market participants. It is important that all persons involved with the information chain during an IPO have a process to identify whether the information they disclose or receive is inside information.

4.18 Article 10(1) of MAR states that unlawful disclosure arises where a person possesses inside information and discloses that information to any other person, except where the disclosure is made in the normal course of employment, a profession or duties.

4.19 Based on the initial evidence we have gathered, as reported in Chapter 2, consideration of obligations under Article 10 of MAR are particularly relevant to information that might be disclosed to analysts, and in turn their audiences, as part of IPO communications. In this context, the three types of information typically disclosed at the analyst presentation, as described in Chapter 2, should be assessed for inside information, particularly the strategic and forward-looking information on the issuer. Issuers should give careful thought to whether any inside information on a prospective IPO has been disclosed in accordance with Article 10(1) of MAR (e.g. 'in the normal exercise of an employment, a profession or duties'). We note that requiring an analyst or other market participant to sign a non-disclosure agreement does not guarantee that disclosure of inside information is lawful in accordance with Article 10 of MAR.

4.20 If inside information has been identified, an issuer must also consider its own announcement obligations under Article 17 of MAR which states that inside information must be disclosed as soon as possible unless there are circumstances under which such disclosure can be delayed. Where disclosure has been delayed, the FCA must be notified when the inside information is subsequently announced (Article 17(4) of MAR).

4.21 Furthermore, issuers or those acting on their behalf, when communicating with potential investors, must consider whether such communications amount to market soundings, as defined in Article 11(1) of MAR and therefore, whether they are fulfilling the obligations set out in Article 11 and whether they wish to take advantage of the protection offered through meeting the sounding regime requirements set out in the associated MAR delegated regulations (Regulation 2016/959 and Regulation 2016/960).

4.22 As mentioned above, it is our view, subject to any communication by ESMA, that all transactions of an issuer which has existing financial instruments admitted to trading on a trading venue, or where a request for admission on to a trading venue has been made, would fall in scope of Article 11 of MAR, provided that the elements of the market sounding definition in Article 11(1) of MAR are met in a given circumstance, and regardless of whether or not the information communicated is inside information.

4.23 In considering whether the offence of insider dealing under Article 14 of MAR could be committed, the provisions of Article 8 and the detailed scope provisions in Article 2 are relevant.

4.24 Once we have considered the feedback, if we consider it is appropriate to give formal guidance on any of the MAR obligations referred to above we will consult in due course.

Q10: Do you have any comments on how/if you think that the handling and disclosure of inside information in the IPO process is consistent with MAR? In particular, if an analyst presentation contains inside information please describe:

- **Why you believe disclosing inside information in an analyst presentation is in accordance with Article 10 of MAR, taking into account that disclosure is being made both to the analyst and the recipient of the analyst's research,**
- **Why you think that the grounds for delaying disclosure of that information under Article 17 of MAR will have been met.**
- **Alternatively, please describe why you believe the information disclosed in an analyst presentation does not amount to inside information as per Article 7 of MAR.**

4.25 In addition to the need to ensure consistency with MAR, issuers and their advisers need to consider their compliance with the broader regulatory framework, particularly in the context of information flows throughout the IPO process, as described in Chapter 2. For example, requirements in the Prospectus Rules, relating to advertisements and all other information concerning an offer or admission to trading needing to be consistent with information contained in the prospectus[13], are likely to be relevant when considering information shared in the analyst presentation or passed verbally to the analysts, particularly strategic and forward-looking information.

13 See PR 3.3.2R and 3.3.4R.

Q11: Are you aware of any aspects of existing market practice that has developed in relation to the current IPO process that may be inconsistent with the broader regulatory framework (for example the Prospectus Rules)? If so, please describe and comment on whether these would be equally relevant to the market practice adopted following our proposed reforms.

Proposed Handbook guidance

4.26 The second policy measure we are proposing is new Handbook guidance clarifying our expectations on analysts' interactions with the issuer's management and their corporate finance advisers around the time an underwriting or placing mandate and subsequent syndicate positioning is being considered.

4.27 Our existing guidance in COBS 12.2.9G states that an analyst should not become involved in activities which are inconsistent with the maintenance of their objectivity. The existing guidance then provides examples of activities which would ordinarily be considered inconsistent with an analyst's objectivity, including participation in investment banking activities such as corporate finance business and underwriting, and participation in 'pitches' for new business. We are proposing to supplement the existing COBS 12.2.9G with further guidance to clarify that we would regard 'participating in 'pitches' in new business' to include where an analyst interacts with the issuer or its representatives until:

- the firm has accepted a mandate to carry out underwriting or placing services for the issuer; and
- the firm's position in the syndicate has been contractually agreed.

4.28 The proposed guidance (see Appendix 1) is intended to reinforce the framework in COBS 12 to further mitigate the risk of bias being imparted to connected research. This should also reinforce the benefits introduced by the new rules described above.

4.29 Given the evidence reported in previous chapters suggesting that the issuer's advisers establish review processes for connected research as a way of controlling the messaging, there may be a case for extending the above proposed guidance to any interaction between analysts and corporate finance advisers during the production of research. We welcome stakeholder views on this as part of our consultation.

Q12: Do you agree that the proposed policy measure helps to address the identified conduct risks associated with the production of connected research, and serves as an appropriate basis for reformed market practice? If not, how should it be amended?

4.30 To minimise potential disruption to existing or prospective IPO transactions, we would expect to allow a sufficient period between the Policy Statement setting out any Handbook changes, and the date at which those changes come into force. We would welcome stakeholder feedback on the appropriate length of this period.

5.
Application of proposals to IPOs on MTFs

5.1 As reported in DP16/3, the timing and sequencing of information for IPOs on MTFs, notably the AIM and NEX Exchange growth markets, is similar to that on regulated markets. This suggests that, in both types of market, the official document on the issuer (i.e. the prospectus or admission document) is available very late in the process, and unconnected analysts lack the necessary information to produce research on the IPO.

5.2 Feedback from the investment banking and institutional investor communities did not differentiate between different types of market. A limited number of stakeholders consider, however, that the current sequencing of information does not create risks in an MTF context in the same way that it does in regulated markets. We were also told that connected research can play a less prominent role than it does in offerings on regulated markets.

5.3 In principle, the proposed rules discussed in Chapter 4, and set out in Appendix 1, could also be operationalised for IPOs on MTFs. Firms providing underwriting or placing services could be prohibited from disseminating connected research until after the publication of a document containing, as a minimum, information on the issuer[14]. The element of the proposed rule providing unconnected analysts with an opportunity to interact with the issuer's management could, in principle, also be applied.

5.4 At this juncture, however, we are not formally consulting on whether the proposed Handbook rules should also apply to firms providing underwriting or placing services in an MTF context. Instead, we intend to use this consultation process to understand in greater detail the similarities and differences between the IPO processes for transactions on regulated markets and MTFs. This would help us to gather further evidence to inform our view as to whether a subsequent separate consultation on this question should be undertaken. If appropriate, this would be launched alongside the Policy Statement for the present CP.

Q13: Is it appropriate to extend our proposed rule to firms providing underwriting or placing services on IPOs on MTFs, notably the AIM and NEX Exchange growth markets? In supporting your answer, please provide details of the following:

- **The sources of information that are currently made available to investors during IPOs on these markets, their role in investor education and price discovery, and a description of the process;**
- **The extent to which current market practice for IPOs on MTFs poses similar or different risks**

14 This could be linked to the content requirements of a share registration document, as set out at Annex I-II of PR App 3.1

to the FCA's operational objectives as market practice for IPOs onto regulated markets, as outlined in Chapter 1;

- Any specific concerns with extending the proposed rules to firms providing underwriting or placing services on IPOs on MTFs.

Annex 1
Cost benefit analysis

1. The Financial Services and Markets Act 2000 (FSMA), as amended by the Financial Services Act 2012, requires the FCA to publish a cost benefit analysis (CBA) of our proposed Handbook rules. Specifically, section 1381 requires us to publish 'an analysis of the costs, together with an analysis of the benefits that will arise if the proposed rules are made'. It also requires us to include estimates of those costs and benefits, unless they cannot reasonably be estimated or it is not reasonably practicable to produce an estimate.

2. As outlined in Chapter 4 and Appendix 1, we are proposing a package of policy measures intended to improve the quality of information available to relevant market participants during the IPO process.

3. This Annex presents the CBA of these proposals. It first outlines the market failure analysis that provides a rationale for the intervention and then presents our assessment of the benefits and costs that we expect as a result of implementing the new Handbook provisions.

Market failure analysis

4. Our evidence points to two forms of market failure. First, there are clear information asymmetries between the issuer, corporate finance adviser and underwriting banks on the one hand, and the prospective investors on the other hand. The corporate finance advisers and syndicate banks advising the issuer may have an incentive to control the messaging of the offering through the dominant role of connected research throughout the process, which is at heightened risk of bias. This means that investors, unlike the issuer, syndicate banks and corporate finance advisers, do not have access to a complete set of information on the company looking to IPO. As a result, investors may make less informed decisions with lower confidence and greater uncertainty, than would be the case if they had more complete information. This may lead to less efficient pricing of the offering[15] and make the IPO process a less cost-effective route for issuing firms to raise capital.

5. The second form of market failure relates to a lack of competition in the production of IPO research. The current practice of both delaying the publication of an approved prospectus and not providing unconnected analysts with an opportunity to meet the issuer's management means that alternative providers of research (e.g. independent research providers or analysts within non-syndicate banks) face very high barriers to produce IPO research. These barriers are reinforced if corporate finance advisers and syndicate banks advising the issuer wish to control the messaging of the offering, which they may perceive as being jeopardised by the involvement of unconnected analysts. This, therefore, prevents any competitive dynamics from enhancing the quality of connected research and prevents investors from accessing a diverse range of views on the offering and the issuer's prospects, reinforcing the detriment arising from the information asymmetries outlined in the above paragraph. Investors' demand for

15 The FCA Occasional Paper 15 examined estimates of the under-pricing of IPOs in EMEA markets. For the period 2010 to May 2015, we reported mean IPO under-pricing to be 4.8% and 5.4% for first day and first week, respectively. Whilst we recognise that there are various explanations for IPO under-pricing, information asymmetries are widely recognised to be an important component.

unconnected research cannot be satisfied even though we expect the cost to issuers and banks to be lower than the value that this research creates for investors (see below).

Analysis of costs and benefits

6. In this section we assess the costs and benefits of our proposals. To do so, we:

- describe the evidence we have based our assessment on
- identify the baseline against which we will assess the incremental benefits and costs, and
- outline the benefits and costs.

Evidence base for the CBA

7. Our CBA has been informed by detailed stakeholder feedback on DP16/3, from both written responses and subsequent stakeholder engagement. We received 36 written responses from a range of stakeholders including investment banks, institutional investors, law firms, corporate finance advisers, private equity houses and various trade associations. We also held a large number of bilateral meetings with these stakeholders.

8. Specifically to inform our assessment of the costs of providing unconnected analysts with access to the issuer's management, we have gathered information on the costs of hiring corporate venues from our Communications Department.

Baseline for analysis

9. The relevant baseline against which we assess the incremental costs and benefits of a policy is the situation without any proposed intervention.

10. In this context, the current typical UK IPO process is outlined above under 'Market failure analysis' and in further detail in Chapter 2 of DP16/3[16]. The existing market practice that is subject to some degree of change as a result of our proposed package of measures are:

- interactions between connected analysts and the issuer's management and corporate finance advisers around the time that an underwriting mandate and subsequent syndicate positioning is being considered
- the size or number of analyst presentations, which takes place around four weeks before the ITF announcement and release of connected research, and
- the late availability of the pathfinder and final approved prospectuses, both of which come after connected research.

11. In terms of establishing the baseline regulatory environment, activities of relevance to our proposals are underwriting and placing and investment research. Since the Markets in Financial Instrument Directive (MiFID) II introduces new requirements in these areas, we have taken the baseline to be the MiFID II standard, noting here that we recently consulted on the domestic implementation of this[17].

Costs of proposals

12. In this section we consider the costs that may result from implementing the policy proposals. We assess the direct and indirect costs to firms and issuers.

16 https://www.fca.org.uk/publication/discussion/dp16-3.pdf
17 https://www.fca.org.uk/sites/default/files/cp16-29.pdf

Costs to firms and/or issuers

13. Our proposals would not materially alter the mechanics of book-build process underpinning UK IPOs, nor would it change the business models of underwriting and placing firms. Rather, they are intended to require incremental changes to market practice.

14. Our proposals would change the three areas of market practice outlined above. Below we assess the extent to which these changes create costs for syndicate banks or issuers.

Re-sequencing the publication of an approved prospectus or registration document and connected research

15. Publishing an approved prospectus or registration document before connected research is released is unlikely to create additional costs for syndicate banks or issuers. This is because, under the UK's current process, the FCA's UKLA Department's current review processes for 'pathfinder' prospectuses, which contain information to be included in a single prospectus or each element of a tripartite prospectus, are largely complete before the ITF announcement and release of connected research. In addition following discussions with various stakeholders we do not expect a material impact on the way due diligence is carried out for eligibility purposes.

16. We do not expect the re-sequencing of an approved prospectus document and connected research to create any additional execution risk. This is because, based on feedback from banks, this aspect of our proposed reforms is likely to result in the publication of an approved registration document up to seven days before the ITF announcement and release of connected research. We were told that this would be specifically intended to prevent any lengthening of the IPO timetable that would constitute a potential cost to the issuer through additional execution risk[18].

17. There may be small one-off compliance costs for banks associated with having to update internal policies and procedures related to underwriting or placing services and the production and distribution of connected research. Banks may also face incremental on-going compliance costs for monitoring compliance with any revised internal policy. We expect this increase in costs to be of minimal significance, but would welcome further evidence from banks.

18. We consider this assessment of costs for firms and issuers would remain whether the issuer or syndicate banks decided to impose either a one or seven-day period of separation between publication of an approved prospectus or registration document and connected research.

Providing unconnected analysts with an opportunity to be in communication with the issuer's management

19. Under our proposals, issuers or syndicate banks have the option to provide unconnected analysts with an opportunity to be in communication with the issuer's management alongside connected analysts[19]. If any such invitation were taken up, and assuming that, in line with existing practice, the mode of communication is a physical meeting through the analyst presentation, perhaps followed by a Q&A session via conference call or email exchange, any incremental costs to the bank or issuer are not expected to be material[20]. This is because the physical meeting and any subsequent communications would have taken place anyway, with the only difference being an expansion of the physical meeting to accommodate additional analysts. Based on information provided by our Communications Department, the variable costs associated with hiring a typical City of London venue would be £8 per person. This would

18 Note that banks consider that a registration document would not necessarily signal that a transaction is taking place in the way that an ITF announcement does.

19 Note that, under this option, syndicate banks would need to impose one day of separation between an approved prospectus or registration document and connected research.

20 The cost would either be capitalised into the fee charged by the bank to the issuer, or directly met by the issuer.

cover the cost of two refreshment breaks over a half-day meeting. Based on a situation where 60-100 unconnected analysts attended, we estimate that banks or issuers face an incremental cost of around £500-£800.

20. Our proposals also allow the issuer or syndicate banks to provide unconnected analysts with an opportunity to be in communication with the issuer's management at a later stage than connected analysts[21]. If any such invitation were taken up, and assuming that the mode of communication is a physical meeting through an analyst presentation (separate to connected analysts), the issuer or banks would incur additional costs for hiring a venue. Based on information provided by the our Communications Department, the total cost of hiring a typical City of London venue for 60-100 unconnected analysts is estimated to be approximately £25,000-£30,000. The estimate is based on a venue being a theatre-style format with stage furniture, five lapel microphones, roving microphones for the audience and the services of a technician throughout. It also includes a webcast. In practice, the cost of hiring this type of venue is likely to be less because it is subject to negotiation to ensure value for money. If, rather than a physical meeting, any separate communication between the issuer's management and unconnected analysts were to be facilitated through one or more web-based communications, conference calls or email exchanges, the above costs would reduce significantly.

21. Where unconnected analysts are in communication with the issuer at a later stage than connected analysts, there is likely to be an opportunity cost arising from the time that the issuer's management and their advisers could have spent doing other business activities. Given that, under our proposal, this communication would need to be scheduled for a time well before the start of the management roadshow, the additional call on the time of the issuer's management and advisers would be small. Assuming a physical meeting and that the attendees are 2-4 members of the issuer's management[22], together with a member of staff from their corporate finance adviser and legal counsel, the opportunity cost might be expected to be around £4,000-£8,000 for a typical IPO. This opportunity cost is likely to significantly lower if the communication was facilitated through one or more web-based communications, conference calls or email exchanges.

22. The proposed rule in Appendix 1 requires syndicate banks to keep a written record of their assessment on how the 'range' of unconnected analysts that are provided with an opportunity to be in communication with the issuer would have a reasonable prospect of enabling potential investors to form an informed view of the company based on a more diverse set of substantiated opinions. We would expect this to create costs of only minimal significance.

23. The above estimates suggest that the total economic costs of providing unconnected analysts with access to the issuer's management could be within a possible range of £500-£38,000 for a typical IPO, showing that costs would be larger if unconnected analysts were provided with management access separately to connected analysts. These costs are very small in the context of the UK IPO market with average new funds worth £107 million being raised for a typical IPO.[23]

24. We would welcome any further evidence from banks on the likely costs associated with the proposed communications between unconnected analysts and the issuer's management.

21 Note that, under this option, syndicate banks would need to impose seven days of separation between an approved prospectus or registration document and connected research.

22 Here we assume that attendees would be the CEO, CFO and up to two additional specialist members of management.

23 Figure calculated on the basis of IPO transactions on Main Market and AIM over the period 2011-2016, using data from the London Stock Exchange's New Issues & IPO summary (http://www.londonstockexchange.com/statistics/new-issues-further-issues/new-issues-further-issues.htm).

Analysts no longer interacting with the issuer's management or its corporate finance adviser around the time that an underwriting mandate and subsequent syndicate positioning is being considered

25. The change is simply bringing market practice in line with what we already expect under the existing COBS 12.2.9G. In any case, we would not expect any costs for banks or issuers to arise from this change.

Benefits of proposals

26. Our policy proposals should generate the following positive outcomes for the UK IPO process:

- An approved prospectus or registration document, a key source of objective information for investors, should be made available earlier in the process than is currently the case and less reliance is placed on potentially biased connected research.
- Two significant barriers to the production of IPO research for unconnected analysts (namely a lack of access to a prospectus and the issuer's management) will be eliminated, therefore, providing the necessary conditions for unconnected analysts to produce IPO research at a stage when it is useful for investors, promoting effective competition in the market and helping to improve the quality of all research and satisfying investors' demand for a third party assessment of the issuer.
- There should be a reduced risk that bias is systematically imparted to connected research, therefore, improving its quality.

27. Benefits will arise from the wider range of higher quality information available to investors, enhancing investor confidence, and allowing them to provide more informed feedback on the company when the syndicate banks are establishing the price range for the transaction. The more informed investment decisions that investors can then make and the reduced uncertainty they need to be compensated for should improve the overall pricing efficiency of the IPO process and ensure a more cost-effective route for issuers to raise capital. This should help to enhance the effectiveness of the UK's capital markets, helping to attract companies to IPO in the UK.

28. Although it is unclear precisely how much unconnected research would feature, any that does emerge would further reduce information asymmetries and create further such benefits. However, for IPOs where no unconnected research is produced, there would be no benefits additional to those outlined in the above paragraph, whilst still creating costs to the syndicate banks or issuers from arranging and staging any unconnected analyst meeting.

29. We consider that the benefits of our proposed policy intervention outlined above cannot reasonably be estimated. This is because, due to the absence of any comparable regime from which the necessary data to produce a reasonable estimate might be obtained, in our view is would not be possible to measure the impact of a wider range of higher quality information (as brought about from our specific proposals) on the degree of investor certainty and the cost of capital for issuers.

30. Responses to the consultation and our engagement with stakeholders have suggested that the publication of an approved registration document or prospectus prior to the release of connected research will have two notable cost-reduction benefits. First, the connected research is likely to become a shorter document and, therefore, less costly to prepare. This is because it would no longer be necessary to include material properly presented through the approved prospectus or registration document. Second, connected analysts would be able to check their

output prior to publication directly against the approved prospectus or registration document, making the due diligence process easier to complete.

Summary of costs and benefits

31. Given that the costs of our policy proposals are estimated to be very small, we expect that benefits will be higher than costs.

Q14: Do you agree with the CBA for our policy proposals as summarised in Annex 1? Do you expect our policy proposals to give rise to any costs and benefits that are not of minimal significance that have not already been considered in the CBA?

Annex 2
List of questions

Q1: Are you aware of any other conduct risks associated with the production of connected research? If so, please describe them.

Q2: Do you agree that connected research should continue to play a role in the UK IPO process?

Q3: Do you agree that simultaneous publication of an approved prospectus or registration document and connected research does not adequately address level playing field issues for unconnected analysts and still leaves connected research excessively prominent in initial price discovery?

Q4: Do you agree that, if unconnected analysts were to be provided with access the issuer's management only at a later stage than connected analysts, there should be a mandatory seven-day period of separation before any connected research could be released?

Q5: Do you agree that this proposed policy measure would effectively advance our objectives of enhancing market integrity, protecting investors and promoting effective competition? If not, how should it be amended? Please explain how your alternative suggestion would advance our objectives.

Q6: Do you agree with the proposed rules set out in Appendix 1? If not, how should they be amended?

Q7: If you think that there are advantages to an alternative approach to the one we had envisaged, please provide details.

Q8: Does this proposal have any practical implications for the transaction review process?

Q9: Do you think that the suggested industry guidelines would help to operationalise the proposed rule requiring syndicate banks to provide unconnected analysts with an opportunity to be in communication with the issuer's management?

Q10: Do you have any comments on how/if you think that the handling and disclosure of inside information in the IPO process is consistent with MAR? In particular, if an analyst presentation contains inside information please describe:

- Why you believe disclosing inside information in an analyst presentation is in accordance with Article 10 of MAR, taking into account that disclosure is being made both to the analyst and the recipient of the analyst's research,
- Why you think that the grounds for delaying disclosure of that information under Article 17 of MAR will have been met.
- Alternatively, please describe why you believe the information disclosed in an analyst presentation does not amount to inside information as per Article 7 of MAR.

Q11: Are you aware of any aspects of existing market practice that has developed in relation to the current IPO process that may be inconsistent with the broader regulatory framework (for example the Prospectus Rules)? If so, please describe and comment on whether these would be equally relevant to the market practice adopted following our proposed reforms.

Q12: Do you agree that the proposed policy measure helps to address the identified conduct risks associated with the production of connected research, and serves as an appropriate basis for reformed market practice? If not, how should it be amended?

Q13: Is it appropriate to extend our proposed rules to firms providing underwriting or placing services on IPOs on MTFs, notably the AIM and NEX Exchange growth markets? In supporting your answer, please provide details of the following:

- The sources of information that are currently made available to investors during IPOs on these markets, their role in investor education and price discovery, and a description of the process;
- The extent to which current market practice for IPOs on MTFs poses similar or different risks to the FCA's operational objectives as market practice for IPOs onto regulated markets, as outlined in Chapter 1;
- Any specific concerns with extending the

proposed rules to firms providing underwriting or placing services on IPOs on MTFs.

Q14: Do you agree with the CBA for our policy proposals as summarised in Annex 1? Do you expect our policy proposals to give rise to any costs and benefits that are not of minimal significance that have not already been considered in the CBA?

Annex 3
Compatibility statement

1. This annex sets out our view on how the consultation proposals and draft Handbook provisions in this Consultation Paper (CP) are compatible with our general duties under section 1B of the Financial Services and Markets Act 2000 (FSMA) and our regulatory objectives set out in sections 1B to 1E of FSMA.

2. We have had regard to the regulatory principles set out in section 3B of FSMA and consider these proposals to be the most appropriate way of meeting our statutory objectives. This meets the requirements on consultation by the FCA set out in section 138I(2)(d) of FSMA.

Compatibility with our statutory objectives

3. In discharging our general functions, our duty is, as far as reasonably possible, to act in a way that is compatible with our strategic objective, to ensure that the relevant markets function well, and to advance one or more of our operational objectives.

4. We consider these proposals are compatible with the FCA's strategic objective of ensuring that the relevant markets function well because they are intended to improve the timing, sequencing and quality of information available to market participants in the equity IPO process. This should help to allow investors to make more informed investment decisions and help to improve the efficiency of the IPO process.

5. We also consider our proposals to advance all three of the FCA's operational objectives. Investor protection should be enhanced when potential investors are able to obtain information contained within a prospectus or registration document instead of being forced to rely on connected research that is at heightened risk of bias. Market integrity should be improved through investors and issuers having greater confidence in the IPO process as a result of price formation being made on the basis of a wider range of higher quality information. Finally, our proposals should enhance effective competition in the interests of consumers because they would remove barriers to the production of unconnected research, therefore, increasing the likelihood that investors can obtain access to a wider range of views on the issuer.

Compatibility with the regulatory principles

6. Section 1B(5) of FSMA requires that, in carrying out our general functions, we have regard to the principles of good regulation. In formulating these proposals we have had regard to the following relevant principles set out in section 3B of FSMA.

The need to use our resources in the most efficient and economic way

7. We believe that the proposals in this CP will have minimal impact on our resources.

The principle that a burden or restriction should be proportionate to the benefits

8. We consider that our proposals are proportionate to the benefits we are seeking. As explained in Annex 2, we expect the incremental costs imposed by the proposals to be very small and, in some cases, of minimal significance.

9. We will continue to engage with stakeholders and welcome comments on these proposals during the three month consultation period.

The desirability of sustainable growth in the economy of the United Kingdom in the medium or long term

10. We consider our proposals to result in a better functioning and more efficient IPO process that should help to enhance the effectiveness of the UK's capital markets, helping to attract companies to raise finance.

The principle that we should exercise our functions as transparently as possible

11. The proposals build upon some initial policy ideas outlined in DP16/3 on the availability of information in the equity IPO process, which was published in April 2016. These ideas were also included in our Investment and Corporate Banking market study interim report, also published in April 2016. We have engaged widely with industry since these publications.

Legislative and Regulatory Reform Act 2006 (LRRA)

12. We have had regard to the principles in the LRRA and to the Regulators' Code when determining general policies and giving guidance. We consider that our proposals are:

- Transparent: We are following a consultation process in making these Handbook changes.
- Accountable: We are seeking feedback on our proposals from stakeholders.
- Proportionate: Our proposed approach has been carefully developed to ensure a sufficient balance between advancing the FCA's strategic and operational objectives on the one hand, and any likely costs that may arise for market participants on the other hand.
- Consistent: Our proposals are applied to firms providing underwriting or placing services.
- Targeted only at cases in which action is needed: We believe that there is a strong case for these measures as discussed in this paper.

Appendix 1
Draft Handbook text

CONDUCT OF BUSINESS (INITIAL PUBLIC OFFERING RESEARCH) INSTRUMENT 2017

Powers exercised

A. The Financial Conduct Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):

(1) section 137A (The FCA's general rules);
(2) section 137T (General supplementary powers);
(3) section 138C (Evidential provisions); and
(4) section 139A (Power of the FCA to give guidance).

B. The rule-making provisions listed above are specified for the purposes of section 138G(2) (Rule-making instruments) of the Act.

Commencement

C. This instrument comes into force on [*date*].

Amendments to the Handbook

D. The Glossary of definitions is amended in accordance with Annex A to this instrument.

E. The Conduct of Business sourcebook (COBS) is amended in accordance with Annex B to this instrument.

Citation

F. This instrument may be cited as the Conduct of Business (Initial Public Offering Research) Instrument 2017.

By order of the Board
[*date*]

Annex A

Amendments to the Glossary of definitions

In this Annex, underlining indicates new text.

Amend the following definition as shown.

registration document	(in *Part 6 rules* and *COBS* 11A) a registration document referred to in *PR* 2.2.2R.

Annex B

Amendments to the Conduct of Business sourcebook (COBS)

[*Editor's note*: The text in this Annex takes into account the changes proposed by "CP15/43 Markets in Financial Instruments Directive II Implementation – Consultation Paper I" (December 2015), "CP16/29 Markets in Financial Instruments Directive II Implementation – Consultation Paper III" (September 2016) and "CP16/43 Markets in Financial Instruments Directive II Implementation – Consultation Paper IV" (December 2016), as if they were made.]

11A Underwriting and placing

General requirements concerning underwriting and placing

…

After COBS 11A.1.4EU insert the following new provisions. The text is new and is not underlined.

11A.1.4A R *COBS* 11A.1.4BR to *COBS* 11A.1.4ER apply to a *firm* that:

(1) has *agreed to carry on regulated activities* for a *client* that is an *issuer* ("the *issuer client*") that include underwriting or placing of *financial instruments*, where:

(a) those *financial instruments* ("relevant securities") are either:

(i) *shares*; or

(ii) *certificates representing certain securities* where the certificate or other instrument confers rights in respect of *shares*;

(b) the relevant securities are intended to be *admitted to trading* in the *UK* for the first time;

(c) the trading under sub-paragraph (b) is intended to be effected by an *admission to trading* on a *regulated market*; and

(d) an approved *prospectus* will be required in accordance with section 85 of the *Act* for the relevant securities; and

(2) is intending to disseminate *investment research* or *non-independent research* on that *issuer client* or those relevant securities before the *admission to trading*.

11A.1.4B R (1) Unless it complies with paragraph (2) a *firm* must prevent its staff involved in the production of *investment research* or *non-independent research* ("the *firm's* analysts") from being in communication with the *issuer client* and/or the *issuer client's* representatives outside of the *firm* ("the *issuer* team").

(2) The *firm* must ensure that a range of unconnected analysts (meeting the criteria in paragraphs (3) and (4)) are given the opportunity (subject to *COBS* 11A.1.4CR) either:

(a) to join the *firm's* analysts in any communication with the *issuer* team that is made or received before the *firm* disseminates any *investment research* or *non-independent research* about the *issuer client* or the relevant securities as described in *COBS* 11A.1.4AR(1); or

(b) to be in communication with the *issuer* team in a way that satisfies the following conditions:

(i) the mode of that communication must be reasonably appropriate for the purposes of enabling those unconnected analysts to receive information from and make enquiries to the *issuer* team, so that the unconnected analysts are able to form a substantiated opinion about the *issuer client* or the relevant securities as described in *COBS* 11A.1.4AR(1); and

(ii) that communication must be completed or substantially completed before the *firm* disseminates any *investment research* or *non-independent research* on the *issuer client* or the relevant securities.

(3) For paragraph (2), an "unconnected analyst" means a *person* other than the *firm* or its staff:

(a) who does not provide the service of underwriting or placing of the same relevant securities to the same *issuer client*; and

(b) whose business or occupation may reasonably be expected to involve the production of research.

(4) (a) The *firm* must:

(i) undertake an assessment of the potential range of unconnected analysts for the purposes of paragraph (2); and

(ii) use that assessment to ensure that the range of unconnected analysts given the opportunity under paragraph (2) is one that, in the *firm's* reasonable opinion, has a reasonable prospect of enabling potential investors to undertake a

better-informed assessment of the present or future value of the relevant securities based on a more diverse set of substantiated opinions, compared to a situation in which the only research available to potential investors is that disseminated by *firms* providing the service of underwriting or placing to the *issuer client*.

(b) For its assessment and opinion under sub-paragraph (a) the *firm* may assume that an unconnected analyst that is given an opportunity to interact with the *issuer* team will publish an opinion on the *firm's issuer client* that will be available to potential investors.

(c) The *firm* must make a written record of its assessment and opinion under sub-paragraph (a) at the time at which it forms its opinion.

(d) The *firm's* record under sub-paragraph (c) must:

(i) set out the *firm's* process for conducting the assessment and forming the opinion under sub-paragraph (a);

(ii) identify the *firm's* staff that were involved in forming that opinion; and

(iii) explain the *firm's* consideration of the number and expertise of the unconnected analysts included in the range.

(e) The *firm* must retain the record made under sub-paragraph (c) for five years from the date on which it is made.

11A.1.4C R A *firm* must ensure that any opportunity given to the range of unconnected analysts under *COBS* 11A.1.4BR(2) is given on reasonable terms.

11A.1.4D E (1) For *COBS* 11A.1.4CR, a term is reasonable if:

(a) it restricts the geographical dissemination of research produced by an unconnected analyst; and

(b) such a restriction does not materially exceed prevailing *UK* market practice for independent research on initial public offerings.

(2) Compliance with (1) may be relied upon as tending to establish compliance with the requirement under *COBS* 11A.1.4CR, but only for the reasonableness of any terms that restrict the geographical dissemination of research.

(3) Contravention of (1) may be relied upon as tending to establish a contravention with the requirement under *COBS* 11A.1.4CR, but only for the reasonableness of any terms that restrict the geographical

dissemination of research.

11A.1.4E R (1) A *firm* must not disseminate *investment research* or *non-independent research* on the relevant *issuer client* or relevant securities as described in *COBS* 11A.1.4AR(1) until after the relevant time in paragraph (2).

(2) The relevant time is:

(a) where a *firm* acts in accordance with *COBS* 11A.1.4BR(2)(a), one *day* after the publication of the relevant document in paragraph (3); or

(b) otherwise, seven *days* after the publication of the relevant document in paragraph (3).

(3) The relevant document is:

(a) an approved *prospectus* regarding the relevant securities; or

(b) an approved *registration document* regarding the relevant securities.

(4) For this *rule*, publication of the relevant document means making the relevant document available to the public in accordance with *PR* 3.2.4R (Method of publishing).

…

12 Investment research

…

12.2 Investment research and non-independent research

…

After COBS 12.2.21EU insert the following new provisions. The text is new and not underlined.

12.2.21A G The phrase "participating in 'pitches' for new business" in Recital 56 to the *MiFID Org Regulation* includes a financial analyst interacting with an *issuer* to whom the *firm* is proposing to provide underwriting or placing services (including the *issuer's* representatives outside of the *firm*), until both:

(1) the *firm* that employs the financial analyst has *agreed to carry on regulated activities* that amount to underwriting or placing services for

the *issuer*; and

(2) the extent of the *firm's* obligations to provide underwriting or placing services to the *issuer* as compared to the underwriting or placing services of any other *firm* that is appointed by the *issuer* for the same offering is contractually agreed and documented between the *firm* and *issuer*.

Amend the following as shown. New text is underlined.

Sch 1 Record keeping requirements

…

1.3G

Handbook reference	Subject of record	Contents of record	When record must be made	Retention period
…				
COBS 11.7A.7EU	…	…	…	…
COBS 11A.1.4BR(4)(c)	The *firm's* assessment under *COBS* 11A.1.4BR (4)(a)	(i) The *firm's* process for conducting the assessment and reaching the opinion under *COBS* 11A.1.4BR (4)(a); (ii) the *firm's* staff that were involved in reaching that opinion; and (iii) an explanation of the *firm's* consideration of the number and expertise of the unconnected analysts included in the	Once the *firm* has formed its opinion under *COBS* 11A.1.4BR (4)(a)	5 years

		range.		
…				

Financial Conduct Authority

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