

UK LISTING REGIME

TO CHANGE OR NOT TO CHANGE, THAT IS THE QUESTION

It is not often that the rules around equity capital markets hit the mainstream papers but that was the case with the release of Lord Hill's report on the UK Listing Review ("Report") in March.

Whilst there appears to be general consensus that the UK listing regime would benefit from reform, the nature and scope of desired change is more divisive. The review was launched by the Chancellor towards the end of last year and, in an encouraging sign, the Report was produced in under 4 months.

The next stage is review by HM Treasury, in consultation with the FCA, with the regulator aiming to publish its consultation paper by the summer.

"The Review has more than delivered and I'm keen to move quickly to consult on its recommendations, cementing the UK's reputation at the front of global financial services."

Rishi Sunak, Chancellor, in response to the release of the Report

Relevance for existing listed companies

The Report is wide ranging, covering both near and longer term recommendations. Much of the press attention has centred on the proposals on dual class share structures, weighted voting rights and the likelihood of London making up lost ground as an attractive listing venue for tech and life sciences founders and SPACs (special purpose acquisition companies).

But, in this briefing, we are focussing on the recommendations which we consider of greatest relevance to companies already listed on the LSE.

Secondary capital raisings

Current regime

Currently a prospectus is required if an offer is made to more than 150 people, excluding institutions, or because 20% or more of the company's shares are to be admitted to trading.

The market volatility and uncertain economic environment of 2020 meant that many otherwise financially robust companies needed to raise funding quickly.

One challenge encountered was the Pre-Emption Group's ("PEG") position that pre-emptive offers be required for raises of over 5% of a company's issued

share capital (plus an additional 5% for acquisitions or specified capital investments). However, the measures introduced by PEG for a time limited period last year afforded companies the flexibility to secure funding of up to 19.9% of their issued share capital quickly and effectively, i.e. through a placing.

However, companies needing to issue a higher proportion of their share capital had to navigate the current framework for rights issues and open offers. This requires the production of a prospectus which needs regulatory approval, with the process from when a company decides to proceed with an equity raising to receiving the proceeds taking two to three months. As the Report pointed out, this brings *"all the associated cost and time implications - while markets moved around [the company seeking funds]"*.

Recommendation to fundamentally review the regime

The simplified disclosure regime for secondary issues which was introduced in 2019 goes some way towards dealing with the challenges, but the Report is right that the prospectus regime would benefit from a fundamental review, such that, amongst other changes, there is further differentiation in the prospectus requirements for admission to a regulated market and offers to the public.

Given the nature and extent of ongoing disclosure requirements that need to be satisfied by existing listed companies, and which are readily accessible to shareholders and potential investors alike, we support the recommendation that consideration be given to allowing further shares issuances to be made by way of alternative, less onerous listing documentation. Accelerated rights issue models, such as those of Australia and New Zealand, differentiate and tailor the documentation requirements and bookbuilding process accordingly between institutional and retail shareholders. This enables the offer to institutions to complete in a few days, as is the case here for a placing, with the offer to retail shareholders being open for longer. We support the suggestion that the UK should look to such models to see whether elements of those could be adopted here.

Extension of relaxation of PEG's limit

Carrying out a fundamental review of the prospectus regime is clearly not a quick process and so there is a question of what can be done in the nearer term to address at least some of the challenges. This is particularly pertinent this year as it is likely that many companies will once again look to the equity markets in the second half of this year, once government support tapers off and is withdrawn, leaving the overall impact of COVID-19 on companies that much clearer.

Whilst not discussed in the Report, one option would be for PEG to make the interim measures it implemented last year permanent, or at least extend them for a further period until the more fundamental review of the prospectus regime is complete. PEG is aware of the challenges and earlier this year sought views from market participants on whether to reinstate the higher 19.9% limit and, if so, subject to what conditions. PEG has not yet announced its conclusion but we are hopeful that change will be forthcoming.

Increasing the prospectus exemption thresholds

Another option is to increase the prospectus exemption thresholds in the context of secondary raisings. Currently an equity offer of over €8 million or to more than 150 retail investors triggers the prospectus requirement. Whilst the Report rightly rejects this as the long term solution, increasing these thresholds would be relatively straightforward to implement and would bring benefits in the shorter term to some, albeit not all, companies depending on the size of equity raise contemplated. We therefore encourage the FCA to consider implementing this swiftly, in parallel to the longer term review.

Greater participation of retail investors

Retail investors have, historically, had limited access to the UK equity market - particularly when compared with its Asian and US counterparts. However, 2020 represented a sea change in the number of placings which included a retail offer, and the market response has been overwhelmingly positive. It is therefore fitting that an entire chapter of the Report is devoted to empowering retail investors.

The Report has highlighted the particular detriment that the existing equity raising and prospectus regime poses to retail investors, and emphasised the need to reconsider requirements that have incentivised companies to exclude retail investors in the past.

Measures to encourage and facilitate retail investment however fall within the category of longer term reform with the Report itself noting that its recommendations *"do not offer a "quick-fix" to the conundrum of engaging and empowering retail investors"*.

Whilst increasing the prospectus thresholds mentioned above would not solve this issue, it would enable companies to include a more substantial retail element in any placing. This is another reason why we encourage the FCA to consider this.

Given the focus in this area, a company's approach to retail investors when carrying out a secondary issue is likely to come under scrutiny. In addition, given that retail investors tend to be loyal and long-term shareholders, many companies have concluded that a diversified shareholder base can act as a useful counterbalance against short-sellers and opportunistic investors, particularly when the market is particularly volatile or where patience is needed for a company's strategy or business plan to bear fruit.

We therefore expect that the recent trend of including a retail offer in placings will continue regardless of the outcome of the policy work in this area.

Rebranding the standard listing segment

For many companies, FTSE inclusion is a critical requirement. This is not possible with a standard listing. The Report concludes that more use should be made of the standard listing segment and, whilst it recommends rebranding to make it more attractive, the Report rightly identifies the lack of FTSE inclusion as the more fundamental blocker. The Report therefore recommends that investor groups develop guidelines on areas they see as important to allow companies on the, to-be-renamed, standard segment to be eligible for index inclusion.

FTSE Russell has indicated that it intends to consult on the eligibility criteria once the FCA has published its proposed changes.

If FTSE inclusion were to become possible, then a move to a standard listing may become more attractive to some companies in the FTSE 350.

Next steps

Whilst some of the Report's other recommendations have not been welcomed by some, those covered in this briefing have broad support from market participants.

There is no certainty which of the Report's recommendations will turn into concrete change and, if so, in what form. However, what is clear is that there will be change in at least some areas.

"The much-needed rebranding of the standard listing segment and the review of the prospectus regime are important steps in achieving a modernised listing regime"

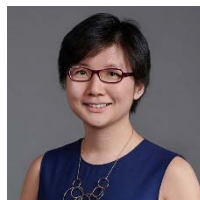
Chris Cummings, Investor Association, 3 March 2021

Companies should monitor developments and ensure that their views are heard as the policy positions are developed. We will be responding to the various consultations that will be launched from the summer onwards and so, if you have any thoughts or suggestions on these topics, please let us know and we will ensure these are reflected within our responses.

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