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IMPROVING ACCESS TO EU CAPITAL MARKETS: FORTHCOMING LEGISLATIVE CHANGES

The European Commission has published near-final versions of legislation designed to simplify EU listing rules, make public capital markets in the EU more attractive for companies and facilitate access to capital, particularly for SMEs. This briefing looks at how the changes will impact equity issuers, particularly those that have a primary or secondary listing of securities on an EU market or that may be considering raising capital in an EU market. It also looks at how UK rules are likely to develop in parallel with EU legislation or diverge away from it. (For details of how the changes will impact debt issuers see our separate briefing.)

Amending legislation

In April 2024 the European Parliament adopted at first reading three pieces of legislation that are part of a package of proposals known as the “EU Listing Act”:

- A proposed Regulation to amend the EU Prospectus Regulation, the EU Market Abuse Regulation and EU Markets in Financial Instruments Regulation (MiFIR);

- A proposed Directive on multiple-vote share structures in companies that seek to list their shares on an EU multilateral trading facility (MTF); and

- A proposed Directive to amend the MiFID II Directive and repeal the 2001 Listing Directive (also known as the Consolidated Admissions and Reporting Directive, or CARD).

Overall effect

On the whole, the proposed changes represent targeted refinements, rather than substantive changes, and have been the subject of lengthy consultation. Many of them are a response to challenges that all capital markets in Europe are facing.

Key changes

- For the purposes of EU MAR, the requirement to announce inside information as soon as possible will not apply where the inside information relates to an intermediate step in a protracted process. Instead, an issuer will have to announce such information only when the process is completed.

- Also for the purposes of EU MAR, it will be made clear that most of the protocols around market soundings – such as the need to obtain the recipient’s consent, inform them that they must keep the information confidential and not use it to deal, and to keep appropriate records - are conditions that must be met for the safe harbour to apply; but it is not mandatory for every market sounding to comply with them.

- All EU MTFs will be required to admit to listing companies that have a multiple-vote share structure (also known as a dual class share structure).

- On EU markets, the minimum percentage of shares that must be in public hands from admission (free float requirement) will be reduced from 25% to 10%.

- Various alleviations will be made to the rules around EU prospectuses, including when a prospectus is required and what information it must include. A path has also been laid down for the EU to recognise a prospectus approved in the UK, US or another third country as equivalent to an EU prospectus.

In the UK, the Government and the FCA are responding to these challenges principally by introducing reforms to the listing regime, prospectus regime and rules around secondary fundraisings; reforms to the market abuse regime may also be brought forward, although probably not for a couple of years. Although in some areas the proposed changes to EU rules will bring them into line with current or planned UK rules, in other areas greater divergence between the EU and UK regimes will inevitably result.

Next steps and timing

We expect the proposed Regulation and Directives to be finally approved substantially in their current form and to enter into force in the second half of this year. Most of the amendments to EU MAR and the EU Prospectus Regulation will take effect immediately; but a few will take effect 15 or 18 months later. In relation to multiple-vote share structures, Member States will have two years to implement the Directive in their national law.

EU Market Abuse Regulation

When inside information arises

The definition of inside information will remain unchanged, but the requirement in article 17 EU MAR to announce inside information as soon as possible will not apply where the inside information relates to an intermediate step in a protracted process. In such circumstances, an issuer will be required to make an announcement only when the final step in the process is taken.

As a result, where there are intermediate steps in a protracted process that is designed to result in a development that would move the share price (such as a large project or transaction), if any intermediate step in the process is “precise” the issuer will have inside information from that point, and would therefore need to create an insider list, prohibit dealings by insiders and take the other usual precautions around inside information. But it will not need to announce the information until the final step in the process is taken - such as when definitive transaction documents are signed or the board gives final approval. Before the final step is taken, the issuer will not be “delaying” making an announcement, so it will not need to satisfy the conditions in the ESMA Guidelines on delaying disclosure.

This change will not take effect until 18 months after the amending Regulation comes into force.

Comment

This change will be helpful to issuers that are subject to EU MAR. However, if an issuer is also subject to UK MAR, and wishes to avoid announcing information about an intermediate step in a process, it will need to get comfortable that the information is not yet sufficiently precise or, if it is, that it can satisfy the conditions for delaying disclosure.

As noted above, we do not expect reforms to UK MAR to be proposed for some time. But when such reforms are eventually considered, the Government and FCA are likely to assess carefully whether to introduce changes that mirror those being made to EU MAR.

Circumstances in which an issuer can delay disclosure of inside information

The current rule in EU MAR that an announcement of inside information can be delayed if, among other things, the delay is not likely to mislead the public (the meaning of which is amplified in the ESMA Guidelines on delaying disclosure) will be replaced with a condition that the inside information does not contradict the most recent previous public announcement by the company on the matter to which the inside information relates.

A new Regulatory Technical Standard will set out a non-exhaustive list of:

- final events in a protracted process and, for each event, the moment when it is deemed to have completed and an announcement must be made; and
- circumstances when inside information contradicts the latest public statement by the issuer on that matter.

The ESMA Guidelines will continue to set out circumstances when an issuer may have a legitimate interest in delaying disclosure, but they will no longer specify circumstances when delaying disclosure would mislead the public.

These changes also will not take effect until 18 months after the amending Regulation comes into force.

Comment

These changes are unlikely in themselves to significantly affect market practice among issuers that are subject to EU MAR. However, it is possible that, when the ESMA Guidelines are updated, ESMA may suggest some changes to the circumstances when an issuer may conclude that early disclosure would prejudice its legitimate interests. In any event, companies that are subject to EU MAR will in due course need to update their policies and procedures around inside information to reflect the changes.

PDMR dealings

The list of exceptional circumstances when a PMDR can deal during a closed period will be expanded. In particular, a PDMR will be able to deal during a closed period where the dealing:

- does not involve any active investment decision or active involvement by the PDMR;
- results exclusively from external factors or third parties; or
- is a dealing based on pre-determined terms.

In addition, the threshold above which dealings by PDMRs and persons closely associated with them (PCAs) must be notified will be raised from €5,000 to €20,000. National regulators will be permitted to raise the threshold to €50,000 or decrease it to €10,000 if justified by specific circumstances.

Comment

In practice, UK-listed companies usually try to ensure that PDMRs do not deal at all during closed periods. Nevertheless, it will be helpful for EU MAR expressly to recognise that some "passive" dealings can be carried out during a closed period (a position that is commonly accepted in the UK).

In relation to the de minimis threshold, in the UK this is generally ignored and instead all dealings by PDMRs and their PCAs are notified - partly due to difficulties with calculating when the threshold has been reached. Similar amendments are therefore unlikely to be made to UK MAR.

Market soundings

Article 11 of EU MAR imposes various rules around market soundings. Broadly speaking, where a company or broker acting on its behalf wishes to disclose inside information selectively to an investor for the purpose of gauging their potential interest in a transaction, it must follow certain protocols designed to ensure that the information is properly safeguarded and not misused. If the protocols are followed, the person will be treated as having disclosed the information in the proper course of their employment, profession or duties and will therefore not commit market abuse by reason of having disclosed the information improperly (i.e. they will qualify for a safe harbour).

There has been debate as to whether all or any of the protocols must be followed for every market sounding (i.e. whether they are mandatory), or whether they are simply conditions that must be satisfied in order for the safe harbour to apply. To resolve this debate, EU MAR will be amended to make clear that:

- Most of the protocols specified in article 11 of EU MAR – including the requirements to obtain the recipient's consent, inform them that they must keep the information confidential and not use it to deal, and to keep appropriate records - are conditions that must be met for the safe harbour to apply; but that it is not mandatory for every market sounding to comply with them.

- The safe harbour is available even if the issuer does not ultimately announce the inside information that was selectively disclosed.

Comment

The first change, in particular, will be helpful. Out of caution, banks tend to assume that all the market sounding protocols are mandatory: this can necessitate careful analysis as to whether a proposed interaction with a key shareholder or other party falls within the definition of "market sounding". Making clear that most of the protocols are not mandatory should therefore remove some of the current friction around such interactions.

Safe harbour for buyback programmes

At present, where a company that is subject to EU MAR conducts a buyback programme, both the company and any bank(s) acting on its behalf will qualify for a safe harbour from certain types of market abuse if the programme satisfies certain conditions. These include requirements to report to regulators and announce to the market specified details of each purchase made under the programme. Some of these reporting and announcement requirements will be simplified.

Comment

This change will reduce the compliance burden for companies and banks and also the risk of a buyback programme not qualifying for the safe harbour due to an inadvertent failure to report all the relevant information.

Proposed Directive on multiple voting rights

Companies with a DCSS to be permitted to list on an EU MTF

Multiple-vote share structures, or dual class share structures (DCSS) as they are more commonly known, are popular with founders of tech and other high growth companies as a way for them to retain control over certain key matters post-IPO without needing to own a blocking minority of the ordinary shares. Essentially the founder is given a separate class of (usually unlisted) shares that carry multiple votes on matters to be decided in general meeting (high vote shares).

In the EU, DCSS are currently exclusively regulated at national level, leaving Member States free to decide what types of structures to permit. For example, they are broadly permitted in Nordic countries and the Netherlands, but prohibited in Germany, Austria and Belgium. The proposed Directive seeks to achieve greater harmonisation among EU Member States - and thus deter companies from "forum shopping" for an IPO venue that permits their desired form of DCSS - by requiring all Member States to ensure that a company seeking to list its shares on an EU MTF for the first time (i.e. doing an IPO) is permitted to adopt a DCSS. Ordinary shares will not have to be given enhanced economic rights as a quid pro quo.

Mandatory safeguards

To provide safeguards for other investors, Member States will have to, among other things, stipulate a maximum voting ratio <u>or</u> require that decisions taken in general meeting require approval by:

- a qualified majority, as specified in national law, both of the votes cast and either of the share capital represented at the meeting or of the number of shares represented at the meeting; or

- a qualified majority, as specified in national law, of the votes cast, and are subject to a separate vote in each class of shares the rights of which are affected.

But this latter alternative requirement will not apply to votes on the appointment and dismissal of directors or "operational decisions to be taken by [the board] which are submitted to the general meeting for approval".

Possible additional safeguards

Member States will also be permitted to introduce further safeguards, including:

- Provisions designed to prevent the enhanced voting rights attached to the high vote shares being transferred to third parties or continuing to exist if the holder dies, becomes incapacitated or retires;
- Provisions stipulating that the enhanced voting rights will terminate if a specified event occurs; and
- Sunset provisions – i.e. provisions stipulating that a DCSS will end after a certain period of time.

Disclosure

Member States will have to ensure that any DCSS (i) is appropriately disclosed in the IPO prospectus; and (ii) is flagged by investment firms and market operators operating an MTF, in accordance with Regulatory Technical Standards that will be adopted by the European Commission.

Comment

The US has relatively permissive rules around DCSS, and a number of high-profile companies with a DCSS have listed in the US over the last few years. In the UK, all types of DCSS are in principle permitted on the standard segment of the Official List, and over the last few years a handful of companies with a DCSS have listed on that segment. Since December 2021, companies have also been permitted to list on the premium segment with a certain limited type of DCSS. On the new ECSS category (which is expected to replace the premium and standard segments from mid-2024), a wider range of DCSS will be permitted: see our briefing for further details.

In the EU, the changes are designed to help attract companies – particularly those led by founders - to list on more junior markets in the EU. As a result, a company looking to list in the EU with a DCSS will have a wider range of markets to choose from, which will increase competition for listings both within the EU and between the EU, the UK and the US.

Repeal of CARD and amendments to the MiFID II Directive

Minimum free float

CARD will be repealed and most of its provisions will not be replaced. However, the CARD requirement for a minimum percentage of shares to be in public hands from admission (free float requirement) will be retained, but with the percentage reduced from 25% to 10%. In addition, it will become easier to satisfy this requirement because eligible investors will count as “the public” wherever in the world they are located - whereas at present they count only if they are located in the EU or EEA. Member States will also be permitted to use other methods of assessing whether there will be a sufficient number of shares to support liquidity.

Investment research

Broadly speaking, the investment research rules in MiFID will be amended to allow the re-bundling of payments for research and execution of orders.

Comment

In the UK, the minimum free float percentage for the standard and premium segments was reduced from 25% to 10% in December 2021. In relation to investment research, the FCA similarly intends to allow re-bundling of payments, so broadly speaking both changes will bring EU rules into line with the UK.

EU Prospectus Regulation

Various changes will be made to the EU prospectus regime to allow companies greater scope to raise new funding without having to publish a prospectus and, where a prospectus is required, to make one easier and cheaper to produce. Some of the key changes are highlighted below.

Exemption from the requirement to publish a prospectus in connection with a secondary issue

At present, no prospectus is required in connection with admission to trading where the new shares represent less than 20% of the shares already admitted (taking into account any shares that were admitted over the previous 12 months). However, a prospectus may be required in any event if the new shares are offered to the public in an EU Member State.

Under the proposed changes, the threshold will be raised to 30%, and the exemption will also be expanded to cover offers of securities to the public. Where an issuer takes advantage of the exemption, it will have to publish a short-form document containing key information for investors, but this will not have to be approved by a competent authority.

Similar amendments will be made to the related exemption for convertibles – i.e. where shares are admitted to trading on a regulated market as a result of the exercise of conversion or exchange rights.

Comment

These changes will make it easier for EU listed companies to do larger fundraisings, including pre-emptive offers, and to use their own shares as acquisition currency, without needing to publish an EU prospectus.

In the UK, the Secondary Capital-Raising Review similarly recommended raising the threshold at which a prospectus is required on a secondary issue, but it suggested the threshold should be raised to 75% (for further details see our briefing). The FCA is yet to decide where the threshold should be set, what type of document, if any, an issuer should be required to publish and whether such document would have to be approved by the FCA.

Exemption for smaller offers to the public

Member States are permitted to exempt domestic offers of securities to the public from the requirement to publish a prospectus where the total consideration to be paid for the securities is less than a specified amount (calculated over a 12-month period). Currently, such amount must be no more than EUR 8 million. This maximum will be increased to EUR 12 million, although Member States will continue to be able to specify a lower threshold. This change will not take effect until 18 months after the amending Regulation comes into force.

Comment

In the UK, the threshold is currently set at EUR 8 million. Under the new regime for public offers and admissions to trading, no prospectus will be required for any offer to the public; but the FCA has proposed that a non-exempt offer above GBP 5 million should have to be made by means of a "Public Offer Platform" (which is expected to be similar to a crowdfunding platform). See our briefing for further details.

Standardising prospectuses

The format and sequence of information in a prospectus will become more standardised, with the European Commission empowered to adopt Delegated Acts covering certain matters of detail. An equity prospectus will have to be no more than 300 sides of A4-sized paper in length. But certain information will not count towards this limit, including the summary, any information incorporated by reference and any additional information that is included because the issuer has a complex financial history or has made a significant financial commitment.

ESMA will be empowered to develop draft Implementing Technical Standards to specify "the template and layout of prospectuses, including the font size, and style requirements, depending on the type of prospectus and the type of investors targeted." ESMA is also expected to develop guidelines on comprehensibility and on the use of plain language in prospectuses to ensure that the information provided is concise, clear and user-friendly.

These changes will not take effect until 18 months after the amending Regulation comes into force.

Simplified prospectus for secondary issues

The simplified disclosure regime for secondary fundraisings by certain issuers will be replaced with a new EU Follow-On Prospectus. This will have to be drawn up in a standardised format and sequence, include certain minimum items of information and be no more than 50 pages of A4 in length. As with an ordinary prospectus, certain types of information will not count towards this limit. This change will not take effect until 15 months after the amending Regulation comes into force.

> ***Comment***
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> *In the UK, no directly equivalent changes have been proposed. But the FCA may consult on the format and maximum length of a prospectus and/or the simplified disclosure regime for secondary issues as part of the forthcoming overhaul of the UK prospectus regime.*

Withdrawal rights

At present, where a prospectus relates to an offer of securities to the public, and the discovery of a significant new factor, material mistake or material inaccuracy necessitates the publication of a supplementary prospectus, investors who have already agreed to purchase or subscribe for the securities have a right to withdraw their acceptance. This right must be exercised within two working days (although an issuer can allow a longer period). Under the proposed changes, investors will be given three working days to withdraw their acceptance.

Six day rule on retail IPOs

Under current rules, where an IPO involves an offer to the public, the prospectus must be made available to the public at least six working days before the end of the offer. Effectively this means the offer must be kept open for at least six working days - a requirement that can deter companies from including a retail offer in their IPO.

Under the proposed changes, the minimum period for which the prospectus must be available in such circumstances will be reduced to three days.

> ***Comment***
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> *In the UK, the Secondary Capital Raising Review (SCRR) similarly recommended shortening the period to three days. The FCA has indicated it is minded to introduce this change, although it is yet to consult on it formally.*

Prospectus equivalence

Under the proposed changes, a third country issuer will be permitted to offer securities to the public in the EU or seek admission to trading of securities on an EU regulated market where it has published a prospectus in accordance with the national laws of the third country (such as the UK or US) provided that, among other things:

- the prospectus has been approved by the supervisory authority of the third country;
- the European Commission has adopted an Implementing Act determining that (broadly) the legal and supervisory framework of the third country imposes prospectus requirements that are equivalent to the EU Prospectus Regulation; and
- the competent authority of the home Member State or, where relevant, ESMA has concluded co-operation arrangements with the relevant supervisory authorities of the third country concerning the exchange of information and the enforcement of obligations.

> ***Comment***
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> *Currently, there is no functioning mechanism for an EU competent authority to recognise a UK prospectus as equivalent, or vice versa. This change may therefore help create such a mechanism, although further steps will need to be taken before it could become operational.*

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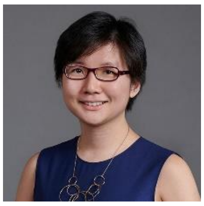

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