FCA Proposes Landmark Reforms to Encourage UK Equity Listings

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Summary

The Financial Conduct Authority (FCA) published an ambitious consultation paper (CP23/10) on 3 May 2023 aimed at creating a more flexible and straightforward listing regime and removing some perceived obstacles to a United Kingdom listing. The goal is to make the UK's equity markets more internationally competitive so as to reverse a decline in UK listings of equity shares in commercial companies.

If enacted, the proposals would create a more permissive listing regime and, in effect, impose more risk on investors. A key aspect would be to streamline the current 'Premium' and 'Standard' equity listing categories for commercial companies into one single category. A number of longstanding Premium listing requirements would be removed entirely, including shareholder approval of certain significant transactions and related party transactions. However, in a number of areas the new requirements would be more stringent than the existing Standard listing regime.

So far, market reception has been mixed but we expect that many, if not all, of the proposals will be introduced given the overall direction of travel. The proposals are therefore likely to be of particular interest to commercial companies with, or considering, a UK listing and existing and prospective investors in such companies.

The consultation closes on 28 June 2023. The FCA intends to issue a further consultation in the autumn setting out its proposed specific revisions to the UK Listing Rules. Subject to the feedback received, the FCA will then look to implement the changes on an accelerated timetable, with "substantial progress" expected by the end of 2023.

One potential outcome is that some issuers currently with Standard listings may become eligible for FTSE index inclusion, with the liquidity benefits that can bring. However, FTSE Russell has said it will not comment substantively on the proposals until the FCA publishes the autumn consultation.

The End of 'Premium' and 'Standard' Listings for Commercial Companies?

The FCA proposes to streamline the current 'Premium' and 'Standard' listing categories for commercial companies into one single equity category with a number of longstanding Premium requirements modified or removed entirely.

In spite of the loss of such protections, the FCA suggests that investors would continue to have the information they need to make initial and ongoing investment decisions, and companies would be expected to continue to engage with shareholders to demonstrate good governance.

Rules that currently apply solely to Premium-listed issuers (such as the sponsor regime, the listing principles and 'comply-and-explain' corporate governance requirements) would be extended to companies with a Standard listing of equity shares but in a more flexible form.

Key Proposals

The FCA has also proposed the following reforms:

1. Initial Public Offering (IPO) criteria: removing the requirement for a three-year financial and revenue earning track record as a condition of listing, and no longer requiring a clean working capital statement.
2. Eligibility: modifying and simplifying the current rules requiring a company to have an independent business and operational control over its main activities by starting from the assumption that companies with substantive corporate structures should be accommodated in the single listing regime as long as they comply with their continuing obligations under the UK Listing Rules. This will create a more permissive approach to accommodate a range of business models and corporate structures such as franchise and strategic investment companies.
3. Class 1 transactions and Related Party Transactions (RPTs): removal of compulsory shareholder circulars and shareholder votes for Class 1 transactions and RPTs but retaining the need for:

- the announcement of key transaction details for Class 1 transactions; and
- a fair and reasonable opinion for larger RPTs.

4. Controlling shareholders: removal of requirement for listed companies to conclude a shareholder agreement with a controlling shareholder by moving to a comply or explain and disclosure-based approach. The current rules for electing independent board members would not change.
5. Dual class share structure (enhanced voting rights): a more permissive form of the current Premium listing regime, which would be subject to a 10 year ‘sunset’ period. This would build on the changes brought in after the UK Listing Review which first permitted such structures.
6. Single Set of Listing Principles: combined and enhanced principles taken from each of the current listing categories. The FCA proposes to retain separate listing categories and rules for equity shares issued by investment vehicles, including closed and open-ended investment companies, Special Purpose Acquisition Companies (SPACs) and potentially other types of investment companies.
7. Sponsor Regime: a modified, streamlined sponsor regime would apply to the new single category, subject to the above changes to significant transaction and related party transaction rules. The sponsor regime does not currently apply to Standard listed companies.
8. UK Corporate Governance Code: the ‘comply-or-explain’ approach would continue to apply in respect of the UK Corporate Governance Code (this would be required for all equity issuers, including those which currently have a Standard listing).
9. Share buybacks/ pre-emption rights/ cancellation of listing: the existing Premium listing rules that regulate share buybacks, the discount at which further shares can be offered on a non-pre-emptive basis, and that require super-majority shareholder approval for de-listings in the absence of a takeover offer would each apply.Body copy is in sentence case. Use lowercase Roman numerals with parentheses to enumerate items. The deal partner requested (i) anonymity, (ii) fee waivers and (iii) rights of first refusal. Paragraphs should be no more than approximately 70 words per paragraph. Use “double quotes” (not ‘single quotes’) in body text. We also use “smart” or “curly” quotes (not straight quotes) globally. Unless employing U.K. English, periods and commas go within quotation marks. “I concur,” she said.[1]

Rationale

There has been growing concern for some time in the City of London around a movement of equity capital markets listings away from the UK. Proposals to improve the appeal of UK equity markets were put forward in

2021 in Lord Hill's UK Listing Review and the Kalifa Review of UK FinTech. While the UK has been Europe's biggest financial hub for many years, UK listings have reduced by 40% since 2008 and 17% since 2015.

Some modest reforms have since been introduced, including a reduction in the free float requirement for a Premium or Standard listing from 25% to 10% and a form of dual class share structure (enabling enhanced voting rights to an extent) within the Premium listing segment, but the trend has continued and, so far this year, London has seen a dearth of IPOs. The London Stock Exchange cited the recent decision by semiconductor giant Arm Holdings to list in the US rather than London, apparently influenced by the UK related party transactions regime, as further evidence of the need for reform.

The FCA is looking to encourage more companies to list, and grow, on UK markets, especially earlier stage, innovative or acquisitive companies in the hope this will create a larger and more liquid market, generating greater investment opportunities and benefitting issuers and investors alike.

The FCA says it has received feedback from market participants that the Premium listing standards, in particular, are overly burdensome, deterring some companies from listing in the UK. However, the new requirements would also be more stringent than the existing Standard listing regime in a number of areas.

The FCA believes the proposals would better align the UK listing regime with other major international listing venues and strengthen the UK's position in global wholesale markets by reducing regulatory burden, adviser costs and streamlining the listing process. Investors would benefit from increased accessibility to a more diverse range of investment opportunities.

FTSE Index Inclusion

The reforms would increase the regulatory burden for companies whose equity shares are currently admitted to the Standard listing segment but may also open up opportunities for these issuers to gain FTSE index inclusion, enlarge their investor base and improve their liquidity.

The FCA has acknowledged that index providers may wish to set higher or different standards for inclusion in their indices, or to create alternative indices reflecting different users' preferences, in light of the proposed reforms. FTSE Russell has said it will not comment substantively on how the proposals will impact the eligibility criteria for the FTSE UK Index series until the FCA publishes its further consultation this autumn.

Market Reception

So far, market reception has been mixed. Some institutional investors view the proposals as simply lowering governance standards and amounting to a backward step for investors. But many participants, not least the London Stock Exchange, have welcomed the proposals as necessary and overdue.

Some, such as Lord Hill, have highlighted the need to focus also on other key factors relevant to a choice of listing venue that would not be directly affected by the proposals. Examples include the pool of capital available, valuations, taxation and executive compensation.

Next Steps

The deadline for responses to the consultation paper is 28 June 2023. The FCA aims to issue a further consultation this autumn with the proposed specific revisions to the UK Listing Rules. Subject to feedback, the FCA is aiming for an accelerated timetable with "substantial progress" by the end of the year.

If you have questions about this client alert, please contact any Akin lawyer or advisor below:

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