

Bear with the FCA – changes are a-comin’

On 29 March 2023, Nikhil Rathi, Chief Executive of the FCA, provided a long-awaited insight into the proposed direction of UK listing reform. The key message was that the FCA seeks to be radical and that change will not be incremental.

The FCA’s thinking appears to have changed significantly over the last few months. The speech emphasises that the new regime will be founded on disclosure, noting the predominance of sophisticated and deeply knowledgeable institutional investors in the UK capital markets who should be allowed the flexibility to form their own judgement when making investment decisions based on issuer’s disclosures. This is a tectonic shift from the current regime where significant shareholder protections (such as shareholder approval for significant transactions) are embedded within the rules.

The FCA acknowledges that it will need engagement from market participants on the detail in order to determine a regime that is fit for the future. Alluding to the story of Smokey Bear, the mascot for the fire prevention campaign, who proved so successful in stopping controlled fires in US national forests and parks that it led to wildfires that wrought more damage, the speech suggests that the UK listing regime has played it too safe over recent years and that this conservative approach has come at a cost to the vitality of the public markets. Obviously, the contrary is also true: policy change can have unexpected consequences and whilst deregulation might free up the market, it could also make it a more risky and less enticing place to invest.

What we know

Key points in the [speech](#) last week include:

- the replacement of the current premium and standard listing segments for shares in commercial companies with a single listing category with one set of requirements (i.e. not the single segment that the FCA previously proposed which had two different sets of obligations for issuers to choose from)
- the removal of eligibility rules requiring a three-year financial track record as a condition for listing as these are not always easy for fast growing start-ups to meet
- a more permissive approach to dual class share structures
- the removal of compulsory shareholder votes for large transactions and for related party transactions, whilst maintaining a disclosure regime
- retaining a sponsor regime (in a streamlined format), a single set of Listing Principles and rules to protect shareholders from the solvent cancellation of a listing without takeover offer or approval by a super majority of investors.

The FCA will publish a “blueprint” for the new regime soon which we assume to mean a consultation paper attaching draft rules.

The tone of the speech and the highlighting of three areas that the FCA would seek to retain suggest that the FCA is striving for a listing regime with fewer rules and which is far less prescriptive. It seems that it will be principles based, and the fact that there was mention of the need for a shareholder vote on solvent cancellation without a takeover suggests that perhaps there will be little else by way of investor protections set down in the rules. The market will set the standards without Smokey Bear to guide it.

And what we don't

The speech was undoubtedly big on ambition but understandably short on detail. It raises a number of questions that will no doubt be answered when we move to the consultation paper but we think are worth careful consideration.

- **Significant and related party transactions.** The suggestion seems to be that there will no shareholder vote required for either a class 1 or related party transaction. This change will help listed companies be more competitive when seeking to make an acquisition or disposal by removing the execution risk around a shareholder vote.

However, it is clear that the FCA will require significant disclosure to be made around a significant or related party transaction. What will this be? In order to ensure that investors have sufficient information to evaluate the transaction and can be confident that once the transaction has completed the company is able to continue to comply with its listing obligations, we think the disclosure may be significant and not too dissimilar to that contained in a class 1 circular. If this approach is followed, careful consideration should be given to what an investor actually needs. In our view, the current disclosure requirements for a circular (in particular the historical financial information requirements) are too onerous and could be slimmed down, saving companies both time and unnecessary costs.

Further, it is not clear what the approach will be on truly transformational transactions. Standard listed equity issuers do not currently need a shareholder vote for reverse takeovers under the Listing Rules, although they are required to publish a prospectus for readmission. Will this be the rule for reverse takeovers for all equity issuers on the Official List going forward?

The FCA reference a streamlined role for the sponsor. It could be inferred that if there is no shareholder vote on a significant transaction or related party transaction, that there will be no role for a sponsor on these transactions. Alternatively, a sponsor (or some other adviser?) could be required to provide a similar service to that which it used to conduct on announcements by premium listed companies undertaking a reverse takeover, which included a declaration on the

issuer's compliance with certain listing requirements and the disclosure provided on the transaction. Without any third-party oversight, will investors be comfortable that they truly understand the implications of a large transaction?

- **Other continuing obligations.** There are a number of other eligibility and continuing obligations that currently apply to applicants and issuers seeking a premium listing that are not alluded to in the speech. For example:
 - Will listed companies have to demonstrate independence / control of business to be eligible for listing? If there is only one segment, the only other UK option for companies not meeting these requirements will be to seek an AIM quotation.
 - Will the restrictions in Listing Rule 9.5 remain in place? For example, will the maximum discount for placings be retained? Will shareholders receive a vote on a reconstruction or refinancing?
 - Will listed companies be required to conduct tender offers for buybacks of 15% or more of the issued share capital?
 - Will listed companies have to comply with the UK Corporate Governance Code?
 - Will the Listing Rules have detailed contents requirements for a company's annual report? The FCA has recently added to these rules to require disclosure around TCFD and diversity, it would perhaps be strange to remove these requirements given the intention to place even more importance on disclosure.
 - Will the controlling shareholder regime be maintained? In particular, will companies with a controlling shareholder need to have special voting requirements for INEDs and relationship agreements with mandatory independence provisions?

All these requirements were introduced to the UK regime in order to “gold plate” a premium listing, raising its standards above those of other EEA regulated markets. Whilst none of them on their own are responsible for creating a perception that the UK listing regime is onerous and too complex, as a package, with the rules for significant and related party transactions, they do not help. However, they also provide investor confidence and we think each should be considered in turn to establish which are worth retaining.

- **Listing Principles.** The highlight given to the Listing Principles suggests that these will sit at the very centre of the new regime. However, it is not clear whether they will be added to, although we think it is fair to assume that all of the eight existing Listing Principles will apply to all listed companies. The obvious risk with a principles, rather than rules, based approach is that whilst focus on the Listing Principles and not specific rules allows more flexibility, it does create a level of uncertainty for all stakeholders as to whether issuers are meeting the expected standards.
- **Dual class share structures.** Given that the FCA recently consulted extensively on changes to the premium listing regime to allow dual class share structures, it will be interesting to see what further “permissive” changes might be allowed. We suggest that the sunset requirements will be removed and founders may well be entitled to near complete voting control. This acceptance of DCSS more than anything else in the speech shows the FCA has bought in to the concept that issuers should be able to arrange themselves as they wish as long as they properly inform the market, which can then make a decision as to whether or not to invest.
- **Existing standard segment issuers.** Whilst it appears that the listing regime will be less onerous than the existing premium listing regime, it may be that companies with an existing standard listing have to make some changes to meet the requirements of the single segment. This may be unappealing to these companies. Whilst there has always been reassurance that different rules will apply to the standard listed companies whose London listing is a secondary listing, the speech makes it clear there will only be one segment and did not touch on how these companies find a home in the new environment and we will have to wait for the

detail to know if these companies will continue to have a ‘London light’ regime or how/when they will be required to adapt.

So whilst the recent speech sets down the direction of travel, there is still much to work through. What is clear is that the FCA is not shying away from ambitious reform and we are in for a wide-ranging debate on the framework for the new listing regime.

It will always be a matter of how best to balance investor protection with creating a vibrant market that allows issuers and investors alike to prosper. The other fundamental question, which is perhaps not for the FCA to answer, is whether change to the listing regime is the answer to why our capital markets are struggling to remain competitive. Increasing investor appetite for public equities will be crucial to increasing valuations and liquidity and making London a more attractive listing venue.

The key will be that all stakeholders buy-in to the reform and that the right balance is struck. London should not want to win a race to the bottom in an effort to show it is open for business. In the 1950s, Smokey Bear appeared on match boxes with the message “Handle with care”. In this respect, we should definitely heed Smokey’s warning.

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