United Kingdom Equity Markets Association (UKEMA) response to the UK Prospectus Regime Review

Introductory comments

In March 2021, as part of a wider debate on the future of the UK's listing regime following the exit from the EU, Lord Hill issued recommendations setting out ways to strengthen the UK's capital markets. He argued that there is widespread support for a review of the UK prospectus regime.

He cited a range of issues raised including the ever-growing size of prospectuses without apparent utility for the reader of the document; detailed disclosure requirements that are inappropriate for many of the companies subject to them, and the fact that these requirements are set out in statute and require an Act of Parliament to change them.

He also cited other problems, including thresholds in current law which discourage listed companies from directing new share issuances at wider groups of investors and advocated a fundamental overhaul of the regime.

With the above recommendations and drivers in mind the members of UKEMA welcome the opportunity to respond to HM Treasury's UK Prospectus Review Regime consultation mindful of the aim of trying to achieve the four main objectives as set out in the paper:

- **Objective 1**: To facilitate wider participation in the ownership of public companies and remove the disincentives that currently exist for those companies to issue securities to wider groups of investors.
- **Objective 2**: To improve the efficiency of public capital raising by simplifying regulation and removing the duplications that currently exist in the UK prospectus regime.
- **Objective 3**: To improve the quality of information investors receive under the prospectus regime.
- **Objective 4**: To make the regulation in this area more agile and dynamic, capable of being quickly adapted and updated as times change.

All too often, companies undertaking fundraisings do not offer any new shares to retail investors because the legal requirement to publish a prospectus where an offer is made to more than 150 persons, and the consequential regulatory burden of publishing a prospectus makes the cost of capital for that portion of the raise prohibitively expensive. This is even more stark within the bond market where little access is available for the retail investor. Practically speaking, the existing rules all too often limit the amount of new capital that an existing listed company can raise and regularly locks out existing shareholders from being able to participate in further equity offerings. In addition, we believe that consideration should be given to allowing the use of prospectuses vetted in other jurisdictions, to meet the primary objectives and allow for wide participation.

Overall, we are pleased and encouraged by both the vision and direction undertaken by HM Treasury in relation to prospectus reform proposals. We support the principle of the differentiating between a public offer and an admission to trading on a regulated market as criteria for the requirement to issue a prospectus. We also strongly support that principle being extended to cover MTFs. We also support the measures being taken to facilitate offers to existing shareholders.

We see that there are significant long-term advantages in enshrining flexibility into the rules governing prospectuses so that UK capital markets can swiftly react and adapt to market practice, and they can generally develop, in line with the objectives set out in the Consultation Paper, over time.

Currently companies admitted to trading on a regulated market raising more than 20% of their existing market capitalisation or issuing more than €8 million of equity capital to the "public" are faced with a complicated and lengthy legalistic process, which is both expensive and time consuming, culminating in the production and publication of a prospectus approved by the regulator.

We understand that HMT Treasury is proposing to remove offers by companies traded on a regulated market for MTF from the public offers regime so that the €8m exemption is no longer required. We agree with HMT that a prospectus should always be required for an IPO given the lack of information about the issuer in the market. However, for secondary offerings, we believe that a separate limit for the exemption from prospectus requirements of at least £20m (i.e., a threshold) is appropriate. Any concerns that this may lead to a significant undermining of the UK's investor protection regime would, in our view, be misplaced.

In short, raising the financial limit would enable companies to raise more capital without being subject to the costly prospectus regime. This could be achieved without any loss of investor protection, whilst achieving most of the objectives as set out in the consultation paper.

In general, we recognise that, if the new prospectus regime is to be capable of being flexible and able swiftly and easily to adapt to market practice and conditions, there is a need to move much of the legal and regulatory framework away from the primary legislature and delegate the more detailed and day to day rule making decisions to other regulators. We have reservations about delegating certain matters to those regulated entities and in others any delegation should not be without a degree of oversight and more public reporting and/or accountability.

We would support the approach to MTFs where MTF Admission Documents are able to be issued directly to the public so as to encourage more public offers on IPOs of companies seeking admission to MTFs furthermore supporting the primary objectives.

Such Admission Documents would be produced under the guidance of the nominated adviser (AIM) or other adviser designated by the rules of the MTF. They would not be subject to FCA scrutiny (or vetting) or approval but would be filed with the National Storage Mechanism.

In a similar vein, we support the proposals for documents making offers to existing shareholders of MTF issuers to be exempt from the public offer regime. Again, we do not believe that such documents should be subject to vetting.

Many practitioners would therefore like to see the vetting procedure dispensed with in many instances. This is particularly the case at the MTF level, where market participants are generally smaller and less well resourced. For such companies, the additional costs and time involved in vetting outweigh any actual or perceived benefits to the issuer.

We strongly support the introduction of measures to facilitate increased disclosure of forward-looking information, such as profit forecasts and estimates, in IPO and secondary issue documentation. Again, we would wish to see these measures apply equally to regulated markets and MTFs. The inclusion of such information could be an important factor in the investor's investment decision.

We strongly support the proposal for offers to existing holders of an issuer's securities to be exempt from the requirement to issue a prospectus under the public offer rules. We believe that this exemption should apply both to issuers on regulated markets and on MTFs. We also see considerable overlap of this exemption with the proposals for a shorter form offering document to replace full prospectuses for all offers made by issuers who are already admitted to trading on a regulated market or MTF and have therefore been subject to the rigorous market disclosure requirements of the Market Abuse Regulation and the rules imposed by their own market operators.

Finally, we encourage HM Treasury to adopt a holistic approach to the review of the prospectus regime as there is considerable overlap with the financial promotion regime set out in the Financial Services and Markets Act 2000. We suggest that this regime is reviewed as well, particularly given the aims set out in Objective 1, as documentation aimed at retail investors is likely to need approving as a financial promotion if the current regime remains in place which will involve banks in additional work.

About the UKEMA:

About the UK Equity Markets Association (UKEMA)

The UK Equity Markets Association (UKEMA) is a newly established and growing group of small and mid-cap investment banks and equity brokerage firms (members are Peel Hunt, Shore Capital, Winterflood, Numis, Arden Partners, Stifel, Liberum and finnCap).

UKEMA members:

- Trade in over 2,000 companies shares (£28.8 trillion in value in the last 12 months), representing 57% of shares traded by volume, and 12% by value of all shares on the LSE.
- Are broker to 782 companies.
- Write research on over 1,700 companies' shares, representing 87% of all UK listed issuers.
- Have raised £6.7bn funds for companies in 2021 so far.

UKEMA looks to increase awareness of small and mid-cap equity investment brokers' value in supporting SMEs to access capital to reach their potential and improve regulation. Indeed, members interact daily with all retail intermediaries and private client wealth managers such as Hargreaves Lansdown, AJ Bell, Barclays Stockbrokers etc.

Some of this is about reducing market access barriers. Regulation also needs to balance providing appropriate protections without being overly burdensome if it's to be effective in attracting listings and help SMEs in particular reach their potential.

This in turn will support the UK's post-pandemic economic recovery, grow the number of listed companies, and increase competition, and helping to make the market more resilient to crises.

What does UKEMA do?

UKEMA's members work together to reduce market access barriers and help policymakers as they develop new frameworks to support and develop the regulation of equity markets. To do this UKEMA seeks to ensure domestic regulation provides appropriate protections without being overly burdensome in order to support public markets and the essential liquidity they provide.

UKEMA supports economic growth

Small and mid-cap equity brokerage firms help SMEs reach their potential, supporting the UK's post-pandemic economic recovery. UKEMA promotes solutions to allow UK equity markets to thrive, supporting the drive to grow the number of listed companies and increase competition, and helping to make the market more resilient to crises.

Chapter 2: Our overall approach

1. **Do you agree with our overall approach to reforming the UK prospectus regime?**

   Yes. We are encouraged by the clear willingness of HM Treasury as set out in the consultation paper to review and challenge the existing prospectus regime which since 2005 has incorporated the EU Prospectus Directive and now the Prospectus Regulation. In our view, the prescriptive nature of the EU regime has discouraged companies from raising capital in the UK capital markets. In particular, as set out in Objective 1, we are keen to encourage retail participation in the UK capital markets. In that regard, we welcome the proposal that offers of securities by companies admitted to trading should not also be subject to the public offer regime (see paragraph 2.16 of the consultation paper).

   We think it is important that there is a holistic approach to consideration of the current UK securities law framework. For example, there is little consideration to the financial promotion regime set out in the Financial Services and Markets Act 2000 in the consultation paper which is a very important part of the current regime which has always been separate from the EU prospectus regime. Further thought should be given to this and, if possible, HM Treasury should consider a review of the financial promotion regime at the same time so that the two regimes are consistent and fit together. This is particularly of concern given the aims set out in Objective 1, as documentation aimed at retail investors is likely to need approving as a financial promotion if the current regime remains in place which will involve banks in additional work and further complexities on transactions which we assume HM Treasury would wish to avoid.

2. **Do you agree with the key objectives that we are seeking to achieve?**

   Yes. In particular, we welcome the aims set out in Objective 1 to encourage retail participation. We also note the aims set out in Objective 4 whilst cautioning that careful thought needs to be given to when primary legislation is appropriate.

Chapter 3: The new FCA powers on admissions to Regulated Markets

3. **Do you have any views on the underlying purpose of a prospectus when seeking admission to a regulated market?**

The legal liability attached to a prospectus is a very important consideration for issuers and their advisors and ensures the accuracy of the information provided and mitigates against the misstatement or omission of key information. On the whole the regulatory review undertaken by the FCA and the statutory liability regime set out in section 90 of the Financial Services and Markets Act 2000 works well and the overall process is designed to protect investors as well as issuers. The 'marketing' aspect of a prospectus (explanation of the business) is important for investors but often forms a secondary consideration after the legal/regulatory role of the document.

4. Do you agree the FCA should have discretion to set rules on when a further issue prospectus is required?

Yes, in relation to regulated markets, noting that we advocate a discretionary and proportionate approach to the application of the prospectus requirements in order to increase and foster the participation in the ownership of public companies in issuing securities to a wider group of investors including retail. HM Treasury should bear in mind that already listed/quoted issuers already publish a significant amount of information pursuant to the UK Market Abuse Regulation and other EU legislation incorporated into UK legislation such as the Transparency Directive together with other UK statutory requirements such as those governing the content of the annual report and accounts.

Careful consideration should be given as to when a prospectus is required and its detailed content requirements. We note that the current rules in relation to admission to trading on a regulated market (derived as mentioned above from EU legislation) require a prospectus to be published on a subsequent issue where the securities represent 20% or more of the existing securities already admitted to trading. In our view, 20% is an arbitrary number and should be increased to 30%, whilst recognising that there is a level at which a transaction is so transformative that a prospectus should be required.

In relation to MTFs, we suggest that market operators such as AIM Regulation and AQSE should be regulating and setting the rules for MTFs, not the FCA.

5. Do you agree the Government should grant the FCA sufficient discretion to be able to recognise prospectuses prepared in accordance with overseas regulation in connection with a secondary listing in the UK?

Yes, the FCA should have discretion, providing the overseas jurisdiction has appropriate equivalence to the UK regulatory regime. We note that although an equivalence regime was established under the European regime, the European Markets and Securities Authority did not put forward suggestions for equivalent jurisdictions and hence there is currently no equivalence regime in practice in the UK. We therefore suggest that this is put in place as soon as possible in order to encourage companies listed in overseas jurisdictions such as Australia and Canada to seek listings in the UK as the current requirement to prepare a prospectus and obtain approval from the FCA is a substantial disincentive to such companies.

Chapter 4: Prospectus content and ancillary provisions

6. Do you agree with our approach to the 'necessary information test'?

Yes, we agree that the core element of the test is well understood by market participants, noting that there is a logic to differentiating between the information required at IPO and for subsequent fundraisings. We agree with the proposal in paragraph 4.9 that a separate test is not required for a further issue, instead it should be a separate factor to be noted.

7. Do you agree the FCA should have discretion to set out rules on the review and approval of prospectuses?

Yes - we agree with the general approach set out in Objective 4 that regulation should be capable of adaption with more flexibility and that in order to achieve this only certain matters should be set out in primary legislation. However, we would encourage the FCA to adopt a proportionate approach to the review and approval of prospectuses as market perception is that in some instances vetting extends the approval process with little discernible benefit. In addition, we note the distinction made between "approval" and "review" in paragraphs 4.21 and 4.23 and would welcome clarification as to how a prospectus can be approved by the FCA if it has not been reviewed. Paragraph 4.21 references the importance of the market and the public knowing, which is the definitive final version of a prospectus, however, if this is the aim we suggest that this could be approved just by filing with the National Storage Mechanism with no FCA involvement at all. Given our comment above about vetting it would considerably simplify matters if there was no review process at all and instead a process similar to the current process for publishing an admission document was adopted.

8. Do you have any comments on what ancillary powers the FCA will need in order to ensure admissions of securities to Regulated Markets function smoothly? (See list of potential powers in Annex A.)

We don't have any substantive comments on the list set out at Annex A.

Chapter 5: Forward looking information

9. Do you agree with our proposed change to the prospectus liability regime for forward looking information?

This seems sensible if the result is to improve the provision of appropriate and high-quality information. Investor protection is paramount, and the balance proposed appears to be appropriate.

10. Do you think that our proposed changes strike the right balance between ensuring that investors have the best possible information, and investor protection?

Yes, we agree that the proposed changes strike the right balance.

Chapter 6: Junior Markets

11. Which option for addressing companies admitted to MTFs do you favour and why?

Our preference would be for Option 2 which whilst appearing more complex than Option 1 gives greater protection to MTF issuers as it would bring them within the statutory compensation regime set out in section 90 of FSMA which does not currently apply to AIM admission documents. However, it is important that the status quo between exchanges and the FCA is maintained as now as set out in paragraph 6.18 and that the FCA does not encroach on the MTF operator's rule making abilities as set out in paragraph 6.16.

Chapter 7: The scope of the UK's public offerings rules

12. Do you agree there should be a new exemption from the public offer rules for offers directed at existing holders of a company's securities? (N.B. Consultation main document omits a Q12 and misnumbers 12-18)

The logic behind such an exemption makes sense as existing investors in a company should be familiar with the company and its recent disclosures (and the risks of investing in the company) but it is important to ensure that issuers are not overly incentivised to only target offerings of securities to existing holders (rights issues) and that a wider investor base (including retail investors where appropriate) can also be allowed to participate.

13. Do you agree we should retain the 150-person threshold for public offers of securities and the 'qualified investors' exemption? Do you have any comments on whether they operate effectively?

We note that the 150-person threshold currently causes problems for retail offers as for example it would require a prospectus for an AIM company to do a rights issue. However, we agree with the conclusion in paragraph 7.13 that the proposals set out in the consultation paper particularly around excluding companies admitted to trading on a regulated market or MTF from the public offers regime will mean that in the future this threshold will only impact private or unquoted companies and therefore we agree that there is no need to change the number.

Although we are in favour of increased retail participation, in practice the "qualified investor" exemption works well for placings, and we wish to retain the ability for placings to be directed solely at institutional investors in circumstances where an offer to retail is not thought to be appropriate.

14. Does the exemption for employees, former employees, directors, and ex-directors work effectively?

This exemption is not as effective in practice as it might be as it requires a document to be made available containing information on the number and nature of the securities and the reasons for and details of the offer which adds further administration.

Chapter 8: Public offerings by private companies

15. Which option for accommodating the right of private companies to offer securities to the public do you favour?

No response

Chapter 9: Public offerings by overseas companies

16. Which of the options above do you prefer? (Please state reasons)

We agree that it should be possible for overseas companies to make offers into the UK without overly burdensome requirements and we are keen for this to be facilitated (see our answer to question 5).

Members would therefore prefer Option 2 and would encourage HM Treasury to do the jurisdictional assessment as soon as practicable given that there has been no equivalence mechanism in the UK since 2005. It is not feasible to maintain the status quo on that basis. We do not agree with Option 3 as we believe that UK investors should have the opportunity to participate in offerings by overseas companies, noting that Option 2 should provide appropriate consumer protection via the jurisdictional assessment being undertaken by HM Treasury.

17. Do you have any further thoughts or considerations over how a new deference mechanism (Option 2) should operate?

No further comments at this stage.

18. Do you agree that there should be no mechanism to allow public offerings of securities by overseas unlisted companies? (Please state reasons) (N.B. Missing from Appendix list)

Agreed as this would pose a significant degree of risk for UK investors without a suitable investor protection regime being put in place. Given that these types of offering would be relatively rare in practice, we do not think this is worth further consideration.