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**Response of the Company Law Committee of
the City of London Law Society to
FSA DP08/01: A Review of the Structure of the Listing Regime**

The City of London Law Society (CLLS) represents over 13,000 City lawyers through individual and corporate membership including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multi-jurisdictional legal issues.

The CLLS responds to a variety of consultations on issues of importance to its members through its 17 specialist committees. This response to the FSA DP08/01 has been prepared by the CLLS Company Law Committee. This Committee is made up of solicitors who are expert in their field.

Introduction

We respond below to the specific questions raised by the Discussion Paper, but first have some general remarks by way of introduction.

The main factor behind this consultation appears to be a concern that the existing listing regime has led to confusion on the part of market participants as to the standards applicable to different issuers. We believe that any such concerns are best dealt with through disclosure, clear labelling and education of investors, financial advisers and investment managers. Achieving a better general level of comprehension of the standards that apply under the different categories of listing should help to ensure that investors are not inadvertently misled, while maintaining the competitiveness of UK markets through the availability of a broad range of listing options. The conduct of business rules also have an important part to play in ensuring that investors are not encouraged to buy securities without appreciating the risks that apply to equity securities of any kind, and, where relevant, the greater risks that may apply in the case of, for example, companies from emerging markets.

Part of the labelling and education process should seek to ensure that there is clarity regarding the regulatory role not only of the FSA and the exchanges, and the nature of the obligations that apply by virtue of admission to listing and to trading, but also of the FTSE Indices. Inclusion in the FTSE UK index series is often more of a prize for an issuer than the status of a primary listing alone, since so many investment mandates - particularly in respect of the vast amount of capital represented by tracker or quasi-tracker funds - are driven by the FTSE indexation of shares. In the case of non-UK incorporated companies, admission to the FTSE UK series is possible subject to the issuer meeting a number of tests relating to control and corporate governance, which ensure certain minimum standards are met by the companies in which tracker finds effectively have to invest. However, the FTSE eligibility requirements are opaque so far as many investors are concerned.

Question 1: Do you consider that the UK super-equivalent Listing standards should be retained?

We believe that the current super-equivalent regime operates well in terms of setting standards which are acceptable to both issuers and investors, and achieving a balance between the UKLA's regulatory objectives of protecting investors and ensuring the competitiveness of the UK's markets. Although not all issuers are able, or wish, to meet the full standards required of a primary listing, in our experience many issuers are willing to opt in to the super-equivalent regime, because of the cachet and correlated access to capital that this brings. Equally, we understand that investors were strongly supportive of the super-equivalent standards when the Wider Review of the Listing Regime was carried out a few years ago, and we imagine that this continues to be the case.

Question 2: Do you consider that the super-equivalent Listing standards should continue to be set by the FSA or should they be determined by the market (exchanges, trade associations or other independent body)?

We can see merits in the super-equivalent standards, particularly those which involve continuing obligations, being set by the FSA. The UKLA is likely to be in a better position to monitor and enforce compliance with continuing obligations because of its experience and regulatory enforcement powers. Some of the current super-equivalent conditions, such as compliance with the model code, are closely related to the market abuse regime. Others, such as the related party and substantial transaction rules, require vetting of circulars, which ties closely in with the vetting of prospectuses. The FSA's enforcement procedures and its powers to censure and fine issuers and their directors provide a regulatory regime which is generally seen as proportionate and effective for purpose. By contrast, an exchange, for example, would not have these powers (and the market would have less trust in regulations aimed at consumer/user protection and market integrity if they were imposed by a commercially motivated body), and its main sanction would be to cancel admission to trading on its market.

These arguments have less force in respect of eligibility requirements which set the threshold to initial listing. A requirement such as the three-year track record does not require ongoing monitoring and arguably sits less well with the UKLA's other functions.

It is worth noting that there are aspects of the overall regime as it currently applies to UK companies that are dealt with outside the UKLA's rules. For example, on pre-emption the Listing Rules provisions have little effect since they merely replicate the company law provisions, but the Pre-emption Group's recommendations in its Statement of Principles have considerable force in the market, despite investor opinion being the only enforcement tool. More fundamentally, inclusion in the FTSE UK Index series is a crucial determinant in many cases of whether an investor will invest in a security or not. We support these mechanisms, as they allow the market to drive best practice and maintain flexibility for issuers.

On the other hand, if super-equivalent standards were devolved to other bodies, the increased fragmentation of the regulatory regime might lead to increased investor confusion and uncertainty. It would be more difficult for investors to determine both the specific rules to which a particular issuer was subject and the standards of regulatory oversight operating to enforce compliance with those rules. This would appear to go against the overall objective of clarifying the listing regime which underlies DP08/1.

Question 3: Should we allow equity securities to be admitted to the Official List if they are only to be admitted to trading on a MTF operated by an RIE or an investment firm and not on a Regulated Market of an RIE? If so, on what basis?

We are not aware of any reason in principle why equity securities should only be admitted to listing if they are admitted to a regulated market operated by a recognised investment exchange. However, we believe a condition of listing should be that the securities are traded on a market that provides an appropriate level of transparency and liquidity.

We consider that the rules that apply to issuers (and others) by virtue of admission to a regulated market - namely the DTR and the PR - are a key part of the listing regime. If they did not apply, broadly equivalent rules would be needed to ensure adequate disclosure is made for the protection of investors. We note, for example, that in the case of securities listed on the Professional Securities Market, which is not a regulated market, the UKLA applies the majority of the DTR and the PR through provisions in the Listing Rules.

The Discussion Paper makes little reference to the Professional Securities Market, which has demonstrated an appetite for listing of GDRs and debt securities by issuers who do not prepare IFRS accounts. We are not clear what the impact on the Professional Securities Market of the proposals discussed in the Discussion Paper would be.

Question 4: Which of the options described above do you consider to be optimal? Please provide the reasons for your chosen option.

We support Option 2 and do not support Option 1.

We consider that Option 1 would reduce choice for issuers wishing to access the UK markets and for investors who wish to invest in securities within the UK regulatory framework. We note that the FSA's regulatory objectives in relation to its primary markets functions include ensuring the competitiveness of the UK markets, and facilitating access to listed markets for a broad range of enterprises as well as providing an appropriate level of protection for investors in listed securities. We believe that Option 1 would not be aligned with these objectives, for the following reasons:

- Those issuers that wished to have an Official Listing of equity without satisfying the full super-equivalent regime would be more likely to seek an alternative listing venue outside London. For UK investors, this would make investment in those entities more difficult, and the competitiveness of the UK markets would be reduced. As stated in the Discussion Paper, it is difficult to quantify either the value attached by investors to Official Listing or the number or value of investment mandates that require securities to be admitted to the Official List (rather than being traded on a regulated market or recognised stock exchange) in the UK. However, there must be a risk that for overseas issuers, without the badge of listing, the range of investors available to issuers would be greatly reduced, and the cost of capital increased, thereby making London no longer a market of choice for such issuers.

- A particular category of investor which may be affected by the proposal is life insurance companies engaged in linked long term insurance business who may only invest in assets that are included in the permitted links set out in the FSA's COBS 21.3.1. One of these categories is "Listed securities" , defined as any security (including a share, debenture or warrant) that is admitted to an "official list". "Official list" is defined as the official list maintained by the FSA as the UK Listing Authority and any corresponding list maintained by a competent authority for listing in another EEA state. This is a narrower definition than a "regulated market" and would mean that life insurance companies would have to examine whether some of their holdings were permitted as "permitted unlisted securities".

- The status of Official Listing enables the FSA to introduce super-equivalent rules where it considers this is appropriate. Although the FSA's general policy stance is to limit superequivalence to primary or "Tier 1" listings, in some areas it already imposes rules beyond the directive minimum. The reserve power to impose super-equivalent measures could be an important element of investor protection in the future.

We do not see any need for substantive change in the structure of the regime and therefore support Option 2. In particular, maintaining the status quo as regards the listing of GDRs and secondary shares avoids the risk of unintended and unforeseen consequences for investors or issuers. By offering a range of listing options to issuers, Option 2 would help to maintain the international competitiveness of the UK markets.

We believe that the objective of protecting investors can be achieved by introducing greater clarity as to what the status of listing does - and, equally importantly, does not - imply. Listing implies that certain rules apply to an issuer but it is not a guarantee of quality. We feel the focus should be on educating investors about the limitations of the concept of listing, and on disclosure by issuers of the rules that apply to them (both under the listing regime itself and, for overseas issuers, under the applicable laws of their own jurisdictions).

Question 5: What are your views about opening up Secondary Listing for UK incorporated companies?

We believe that the availability of choice of listing regimes (alongside AIM, the London Stock Exchange's new Specialist Funds Market, and other UK markets, such as PLUS) is a significant contributor to the UK's importance as a leading financial centre, and should continue to be encouraged and enhanced. For this reason, we would in principle support offering further choice by making secondary (Tier 2) listing available to UK equity issuers if there were demand for this from issuers and investors. Moreover, we do not see any justification for a UK incorporated company operating under the Companies Act 2006 (and therefore subject, for example, to the obligations to publish an enhanced business review and directors' remuneration report) being at a disadvantage to a company incorporated in, for example, a tax haven jurisdiction without these company law features.

On the other hand, we recognise that market forces (such as the greater benefits to be gained from a listing if accompanied by inclusion in the FTSE UK index series, which requires a primary listing) may make this a relatively unattractive option, at least for issuers who would be eligible for the FTSE indices. It is also obvious that as this would be a novel category, it would need to be made clear to investors that UK companies could be within more than one listing category (in addition to AIM). Since the AIM requirements would in some respects be more onerous, the distinction between this type of listing and AIM would also need to be made fully transparent.

Question 6: What are your views on how the provisions we have described above under core requirements should apply to overseas Primary Listed companies?

We recognise the importance of pre-emption rights and compliance with the Combined Code to many investors. However, focusing on those issues misses a fundamental issue, which is that there are many other respects in which an overseas company will differ from a UK company. We agree with the point made at paragraph 6.20 of the Discussion Paper that a “comply or explain” statement will provide false comfort if the company law applicable to the issuer does not offer the same shareholder rights as UK law. We believe that the current obligation on an overseas company to report on the ways in which its actual practices differ from the Combined Code is sufficient. The goal of increased transparency regarding the governance of non-UK issuers would be better served by more general disclosure regarding the rights of shareholders, the responsibilities of directors and other shareholder protections, and how these differ from the corresponding UK provisions.

Question 7: Should we require the appointment of a sponsor for a transaction involving the issuance of GDRs? If not, are there any other responses to the significant growth in GDRs that are necessary?

We believe that requiring a sponsor for GDRs is inappropriate, given that the GDR regime is aimed at professional investors. The disclosure standards and the responsibility rules that apply to GDR issuers have been determined on this basis, and are less than those that apply to listings of shares (including directive-minimum listings). It would merely confuse the distinction between the different categories of listing for a feature of the primary share listing regime to be applied to GDRs when GDRs are in other respects subject to a lighter regime than directive-minimum listings of shares.

We believe that the current regime for GDRs offers a convenient route for UK investors to access securities of emerging market issuers. GDRs give investors the advantage of being able to trade and settle more easily, and this must be preferable to forcing investors - if they wish to take advantage of the opportunity to invest in that entity - to buy the shares on an overseas exchange. Making GDR listing more onerous would very likely result in GDR issuers simply opting for admission to another EEA or non-EEA market for GDRs or listing shares on their home or another exchange. This is likely to be disadvantageous to those UK investors who wish to invest in those entities, compared with having such entities as UK home state issuers, subject to regulation by the FSA.

The intention of the EU directives on listing and admission to trading is to encourage a pan-European trading market and London is part of increasingly global markets. In this context, investors are increasingly seeking investment opportunities in major economic entities regardless of their location of listing. Attracting such issuers to the UK markets must be to the benefit of the UK markets, UK investors, and the reputation of the UK as a financial centre.

To the extent that there are investor protection concerns relating to GDRs in general, we consider the focus should be on disclosure in prospectuses, clarification of the listing regime and appropriate conduct of business rules to prevent mis-selling.

Question 8: Do you have views on the labelling options?

We accept that the terms “primary” and “secondary” listing may be confusing and we would support the removal of these labels. Rather than applying a single label to listings of GDRs and directive-minimum shares, it would also be preferable, given the differences in the rules that apply to them, to make this transparent by giving separate labels to these two regimes.

The label “Tier 1” is also used in the regulatory capital context, and therefore potentially gives rise to scope for confusion.

The clarification of the regulatory framework should recognise that the listing regime will not achieve uniform standards for all issuers, regardless of nationality. The underlying laws of the different jurisdictions where issuers are incorporated have an important bearing on corporate governance and investor rights. Rather than attempting to force a wide variety of issuers into a limited number of pigeon holes, the regulatory framework can, with appropriate disclosure, offer flexibility and freedom of choice to both issuers and investors. The standards of regulation applicable to an issuer are one of the factors, alongside the issuer’s financial and other disclosures, which should be taken into account by investors when making their investment decisions.

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