Capital Markets Alert

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NYSE Direct Listing Rules Approved; Nasdaq Proposes Substantially Similar Rules

If you have any questions regarding the matters discussed in this memorandum, please contact the attorneys listed on the last page or call your regular Skadden contact.

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On December 22, 2020, the U.S. Securities and Exchange Commission (SEC) approved a proposal by the New York Stock Exchange (NYSE) that allows companies going public via a direct listing to issue new shares and raise capital without involvement of a traditional underwriter. The SEC first approved the proposed rules on August 26, 2020, but stayed the approval upon receiving notice that the Council of Institutional Investors intended to petition for review of the rules. After a *de novo* review, the SEC approved the rules, concluding that the NYSE had "met its burden to show that the proposed rule change is consistent with the Exchange Act." The NYSE rules, which are immediately effective, bolster direct listings as a potentially attractive alternative to traditional underwritten initial public offerings (IPOs).

Nasdaq also recently filed a direct listing rule proposal with the SEC, which would have provided for more pricing flexibility than is permitted in the NYSE rules, but the SEC staff delayed approval of the rule, subjecting it to additional procedures for consideration. Upon approval of the NYSE rules, Nasdaq filed a substantially similar proposal, requesting immediate effectiveness. The Nasdaq rules are still awaiting SEC approval.

Background

Historically, both the NYSE and Nasdaq have permitted direct listings as an alternative route to going public for a limited number of companies that, instead of offering shares or raising capital on their own behalves, sought only to register shares held by preexisting investors, enabling them to sell their shares to the public through a resale registration statement. Though direct listings offered certain potential advantages to IPOs, the prohibition on raising new capital along with the significant valuation requirements imposed on companies seeking to list directly were difficult for all but a small minority of companies to meet.

NYSE Rules

The NYSE rules recognize a new category of "primary direct floor listing," permitting companies to raise capital directly, provided certain requirements are met. In particular, companies need to meet higher market valuation requirements and satisfy the NYSE's existing initial listing requirements, which may be more difficult to satisfy within the context of a direct listing than an IPO.

To ensure a sufficiently liquid trading market in the absence of the pricing support and stabilization measures traditionally available in underwritten public offerings, companies engaged in a primary direct floor listing would need to either sell $100 million in shares in the opening auction on the first day of trading, or meet a market valuation of publicly held shares immediately prior to listing of $250 million, compared with the $40 million market valuation that currently applies to traditional IPOs.

Companies seeking to directly list would also immediately have to satisfy the NYSE's initial listing requirements, including that companies have at least 1.1 million publicly held shares, 400 round lot holders (on the NYSE, holders of 100 shares) and a price per share of at least $4.00. These thresholds may be challenging for many private companies to satisfy without the assistance of underwriters, which in a traditional IPO ensure these requirements are met prior to listing through the book-building process. The NYSE rules also require that issuers disclose in their registration statement the number of shares to be sold and a price range. The opening auction price must be within the disclosed price range. An issuer would be required to file a pre-effective amendment to the registration statement if the opening auction price was below the bottom end of the disclosed price range, which compares unfavorably to a traditional IPO, where an issuer conditionally can price outside the price range disclosed in an effective registration statement.

Nasdaq Proposed Rules

The Nasdaq proposal is substantially similar to the NYSE rules and if approved would similarly permit "direct listings with a capital raise" provided that an issuer sell $100 million-$110 million of securities in the opening auction or have a market value of publicly held shares immediately prior to listing of $250 million. Issuers in a direct listing would be subject to the standard Nasdaq distribution requirements (1.25 million publicly held shares, 450 round lot holders or 2,200 total shareholders and a price per share of at least $4.00). Direct listings with a capital raise on Nasdaq also would be subject to identical price range and auction mechanics as primary direct floor listings on the NYSE.

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