

New UK IPO Rules Encourage Independent Research, Address Perceived Conflicts of Interest

Contributing Partner

Danny Tricot / London

Associate

Richard Ho / London

This article is from Skadden's 2019 Insights.

This memorandum is provided by Skadden, Arps, Slate, Meagher & Flom LLP and its affiliates for educational and informational purposes only and is not intended and should not be construed as legal advice. This memorandum is considered advertising under applicable state laws.

Four Times Square
New York, NY 10036
212.735.3000

In July 2018, changes came into effect to improve the range, quality and timeliness of information available to the market and to remedy certain perceived conflicts of interest during the U.K. initial public offering (IPO) process. The new rules have met the U.K. Financial Conduct Authority's (FCA) policy objectives of ensuring the availability of information to the market earlier in the IPO process. Generally speaking, investors now have an additional week to review and consider the registration document and announcements that the issuer publishes before considering research reports, thus supporting a more meaningful investor education and price formation process.

The new rules also have responded to buy-side demands for the production of independent, or unconnected, research, while respecting the value that certain market participants place on connected research. However, initial take-up by unconnected analysts has been low, and it remains to be seen if broader independent research will become commonplace in the future.

Past Practice

Prior to these changes, the FCA-approved prospectus was published by an issuer late in the IPO process. The primary source of information available to the investor community was research reports published by analysts connected to syndicate banks underwriting the IPO. Unconnected analysts generally were excluded and lacked access to the issuer and information needed to produce independent research.

Additionally, perceived conflicts of interest arose because connected analysts often met with the issuer and participated in pitching activities prior to the issuer awarding an IPO mandate. This resulted in concerns that connected analysts would convey positive research messages to the issuer in order to secure an underwriter appointment or a particular position within the underwriting syndicate.

As a result, the FCA was concerned that investor education and the price discovery process were based in large part on connected research that was potentially biased and prepared with a view to ensuring a successful IPO.

New Rules

The new rules are aimed at:

- restoring the centrality to the IPO process of an approved disclosure document;
- creating the conditions for independent research to be produced during the IPO process by establishing a level playing field for connected and unconnected analysts; and
- addressing perceived conflicts of interest relating to interactions between connected analysts and issuers in the pitching and appointment stages of the IPO process.

Under the new rules set out in the FCA Handbook's Conduct of Business Sourcebook:

- Syndicate banks must undertake an assessment of the potential range of unconnected analysts able to produce research on the issuer and ensure that such analysts have the same level of access to the issuer and are provided

with identical information as connected analysts without unreasonable restrictions;

- Issuers must publish an FCA-approved registration document or prospectus before the publication of any connected research;
- Connected research may be published one day after the publication of the FCA-approved disclosure document if unconnected analysts are given access to the issuer at the same time as connected analysts, or after seven days if unconnected analysts are given separate access to the issuer; and
- Connected analysts are prohibited from participating in pitches and may only interact with the issuer after the appointment of the syndicate bank has been confirmed in writing.

Emerging Trends Under New Rules

Since the new rules came into effect, a number of issuers have completed their IPOs, with notable trends and market practices beginning to emerge.

Unconnected Analysts

All issuers have opted to provide separate access for unconnected analysts after the approved registration document has been published. This practice is expected to continue, given the overriding concern about maintaining the confidentiality of the IPO before it is announced. Many issuers continue to seek to control — to the extent possible — the narrative around their IPO, which is easier to do when access to the unconnected analysts is left until later in the process.

In addition, despite the level playing field resulting from the new rules, the number of unconnected analysts who have registered to receive information and subsequently published independent research during the IPO process has been limited.

Registration Document and Prospectus

A prospectus can take the form of a single document or a compilation of three separate documents: a summary, a registration document and a securities note. The registration document contains information about the issuer, including business disclosure and risk factors, and the securities note contains information about the securities and offering.

Although the new rules provide issuers the option to publish either an approved registration document or a prospectus prior to the publication of connected research, it is not possible to produce a full prospectus containing all required information at the start of the IPO process. Issuers therefore have opted to publish a registration document at the start. They also have opted to publish a single, approved prospectus later in the process that contains all relevant information on the issuer and offering, as investment banks have generally considered this preferable from a marketing standpoint.

Announcements

Issuers have traditionally published an intention to float (ITF) as the first public announcement of their IPO. The ITF contains summaries of the issuer's business, strengths and strategies, management, and key offering information.

While no regulations require publication of an ITF, the FCA indicated during the consultation process that it expected issuers to publish the ITF on the date that connected research is published (typically seven days after publication of the registration document). This would mean that the registration document is published in isolation. As a result, issuers have opted to publish a “pre-ITF” announcement on the date of the

registration document, providing in it context for the registration document and guiding the narrative for the potential IPO. The pre-ITF announcement contains a summary description of the issuer, its preliminary intention to carry out the IPO and an invitation to unconnected analysts to register to receive information, but it omits information specific to the offering. On the date of publication of connected research, issuers have published a further announcement confirming their intention to proceed with an IPO, providing details of the offering and any updates to the pre-ITF announcement. The bifurcation of the ITF is expected to continue and supports increased issuer engagement with the market.

Conclusion

Although notable trends and market practices have begun to emerge, the number of IPOs coming to market has been limited due to market conditions and uncertainties surrounding Brexit. In addition, while organizations such as the Association for Financial Markets in Europe have published guidance and process papers on the new rules, each underwriting bank may have its own internal compliance policies for the new rules. As such, practices are likely to continue to evolve.

[Click here for a full list](#) of capital markets-related articles authored by Skadden attorneys in the last year.