

CAPITAL MARKETS UPDATE – PROPOSED CHANGES TO THE AIM RULES AND THE NEW INTERNATIONAL SECURITIES MARKET OF THE LONDON STOCK EXCHANGE

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The past few months have seen some interesting developments in the area of capital markets. In this second briefing of a series of two, we look at the proposals for amending the AIM Rules for Companies (the “AIM Rules”) and the new International Securities Market for debt securities launched by the London Stock Exchange (the “LSE”). In the first briefing, we looked at the new EU Prospectus Regulation.

PROPOSED CHANGES TO THE AIM RULES

The LSE has published a discussion paper on proposed changes to the AIM Rules and the AIM Rules for Nominated Advisers (“Nomads”) (“Nomad Rules”). Responses are requested by 8 September 2017. The key areas under consultation relate to admission criteria and appropriate levels of corporate governance. Feedback is sought on:

Admission criteria

- Codifying and extending to all applicants a requirement that Nomads engage in confidential discussions with the LSE at an earlier stage, to provide information about the company and its proposed admission. Currently, Nomads are required to approach the LSE at an early stage of a new application where atypical features or potential issues may be of interest to the LSE. The LSE proposes to extend this practice to all AIM applications with a view to preventing a delay in, postponement or withdrawal of, a proposed
- Inclusion in the Nomad Rules of a non-exhaustive list of issues that may give the LSE cause for concern and, if unaddressed, may lead to the use of its discretion to refuse, or impose conditions, on admission.

The proposed non-exhaustive issues to be included are as follows:

- Concerns as to the good character, skills, experience or previous history of a director, key manager, senior executive, consultant or
- Where the rationale for seeking admission to AIM is not
- Formal criticism of the applicant and/or any of its directors by other regulators, governments, courts, law enforcement or exchange
- The applicant has been denied admission to trading on another platform or

- Corporate structure and business models that give rise to concerns regarding appropriateness for a public
- Where the applicant holds a derivative or economic interest in a material part of its assets or business operations via potentially risky contractual arrangements with the owner of the assets or operations, rather than by owning them itself or through a subsidiary.
- Whether to prescribe a minimum free float The LSE does not currently consider it appropriate to set a prescribed threshold for the size of free float or the number of shares in public hands, but is asking for views on this.
- Extending to all applicants (or just to non-revenue generating companies) the current requirement that an investing company has to raise minimum funds by way of an equity fundraising on, or immediately before, admission. Although the LSE does not propose to introduce a minimum overall size of applicant requirement, it believes a minimum capital raising threshold would be beneficial as, if set at an appropriate level, it would require external investors, likely institutional investors, which should add extra scrutiny over the business proposition. The LSE also suggests that a minimum fundraising threshold could translate into better quality trading in the secondary market.

"EXTENDING TO ALL APPLICANTS THE CURRENT REQUIREMENT THAT AN INVESTING COMPANY HAS TO RAISE MINIMUM FUNDS BY WAY OF AN EQUITY FUNDRAISING ON, OR IMMEDIATELY BEFORE, ADMISSION"

Views are sought on what an appropriate threshold might be and examples are given of between £2m and £6m (or more). The current threshold is £6m for investing companies.

Corporate governance

- Whether the existing requirement for Nomads to assess the efficacy of a board at admission is effective and whether the AIM Rules should require a specific board composition such as a specified number of non-executive directors. In the LSE's view, only in exceptional circumstances should a board not contain the roles of chairperson, finance director and non-executive
- Whether the existing corporate governance disclosure requirements are adequate, or if it should be mandatory for AIM companies to comply and explain against an industry code of their
- Potential automatic fines for explicit breaches of the AIM Rules, the level of any such fines and the scope of the breaches to be The LSE has suggested that breaches such as late filing of accounts and non-disclosure of AIM regulatory information on a company's website could fall within this regime.

The new International Securities Market of the LSE

In May 2017, the LSE launched the International Securities Market (the "ISM"), a multilateral trading facility ("MTF") that will operate alongside the LSE's Main Board and Professional Securities Market for primary debt issuance. According to the LSE, approximately 15,000 debt instruments are actively traded on LSE's fixed-income market with mor

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The ISM has been designed “to meet the demands of issuers and investors to improve the effectiveness and competitiveness of the UK primary debt markets”. The ISM will compete with Dublin and Luxembourg and meet demand from UK and international debt issuers wanting to gain access to “London’s uniquely deep pool of international capital”. The ISM is aimed at institutional and professional investors.

The key features of the ISM are:

- **Admission standards** – as an MTF and not an EU-regulated market, the ISM will be outside the scope of the EU prospectus. Accordingly, issuers that restrict their offer of debt securities to qualified investors, or that offer such securities in high denominations, will be able to rely on relevant exemptions and not be required to publish a prospectus approved by the UK Listing Authority. Therefore, they should save time and expense in connection with the debt issuance.
- **Simplified requirements for admission to trading** – in order to apply for admission of debt securities to trading on the ISM, an issuer will need to prepare admission particulars in accordance with the London Stock Exchange’s

International Securities Market Rulebook (the “ISM Rules”). The application for admission will be approved by the LSE and not the UK Listing Authority as is the case for the Main Board and the Professional Securities Market.

The ISM Rules incorporate simplified administrative and disclosure requirements and no listing agent is required. Issuers must have published audited financial statements that cover at least two years and the latest financial statements must be in respect of a period ending not more than 18 months before the date of the admission particulars. In some limited circumstances, issuers may have financial statements relating to a period shorter than two years.

The application for admission to trading must relate to all debt securities of that class issued or to be issued after admission if fungible with the securities admitted. The expected aggregate market value of the debt securities to be admitted (except for securities that are already admitted) must be at least £200,000 (although, securities of a lower value may be admitted if there will be an “adequate” market for such securities).

Convertible securities may be admitted to trading if the securities into which they are convertible or over which they give a right to buy/subscribe are already, or will become at the same time, admitted to trading on a suitable market that includes all LSE’s markets, regulated markets and any exchange/MTF deemed suitable by the LSE.

- **Continuing obligations** – an ISM issuer will be obliged to consider its obligations under the EU Market Abuse Regulation, which applies to MTFs. Once admitted to trading, an issuer must ensure that all holders of securities are given equal treatment in respect of all the rights attaching to the securities. The issuer must publish information without delay relating to, among other things, any changes in the rights of holders to the securities, the redemption or cancellation of the securities, any payment default and more generally, any decision relating to bankruptcy, insolvency or cessation of payments.

The LSE has been keen to highlight that it will use a “customer-centric” approach towards admission applications. Debt specialists have been put in place to work with issuers on a collaborative basis and will deal with any questions before a formal application is made. Specific competitive timeframes have been given for the LSE to respond to draft admission particulars; three days for initial comments and two days for subsequent comments.

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In May 2017, The National Power Corporation (India's state run thermal power company) became the first issuer to list debt securities, a masala bond, on the ISM raising INR20bn (US\$4bn).

In order to make UK debt markets focussed on institutional investors more competitive, the UK Government announced in its March 2017 Budget its intention to exempt from withholding tax interest on debt traded on MTFs. Currently, the Quoted Eurobond Exemption removes the requirement for companies to withhold tax at the basic rate of income tax (currently 20%) for interest arising in the UK made by a company on debt listed on a "recognised stock exchange". However, debt traded on UK MTFs does not fall within the exemption, but debt listed on MTFs in Dublin and Luxembourg is covered by the exemption. This gives rise to the perverse situation where UK issuers, to avail of a UK tax exemption, are encouraged to list relevant debt securities on MTFs designated as "recognised stock exchanges" in overseas markets, which leaves London at a competitive disadvantage. HM Revenue & Custom has issued a consultation paper on the proposed changes, whereby a company will not be required to deduct income tax from any interest payment on an interest bearing security admitted to trading on an MTF operated by a recognised stock exchange regulated in an EEA territory. The consultation closed on 12 June 2017 and HM Revenue & Custom intends that relevant legislation should take effect from April 2018. This change will increase the competitiveness of the UK primary debt markets and should stimulate growth in UK MTFs including ISM.

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