ICAEW
REPRESENTATION 30/24

PRIMARY MARKETS EFFECTIVENESS REVIEW CP 23_31

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ICAEW welcomes the opportunity to comment on *Primary Markets Effectiveness Review,* published by the FCA on 20 December 2023, a copy of which is available from this link.

This response of 22 March 2024 has been prepared by the ICAEW Corporate Finance Faculty. The Corporate Finance Faculty is ICAEW's centre of professional expertise in corporate finance. It contributes to policy development and responds to consultations by international organisations, governments, regulators and other professional bodies. It provides a wide range of services, information, guidance, events and media to its members, including its highly regarded magazine Corporate Financier and its popular series of best-practice guidelines. The faculty's international network includes member organisations and individuals from major professional services groups, specialist advisory firms, companies, banks and alternative lenders, private equity, venture capital, law firms, brokers, consultants, policymakers and academic experts. More than 40 per cent of the faculty's membership are from beyond ICAEW.

For questions on this submission please contact the Corporate Finance Faculty at CFF@icaew.com quoting REP 30/24.

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KEY POINTS

High standards are necessary in a disclosures-based regime

1. ICAEW appreciates the FCA's efforts to engage with and invite detail behind different views in the market as it developed and when it published the proposals in consultation paper CP 23/31. Our members are broadly supportive of the concept of a disclosure-based regime providing it is underpinned by high standard and quality disclosure. In our review of the proposals we have focused on minimum standards that issuers should meet in order that investors (and the market) have access to the information they need and to make an informed investment decision, and for the integrity of the market to be maintained.
2. It is generally acknowledged that the proposed regime involves rebalancing of risk - passing greater risk to investors. Accordingly, the quality and governance standards of disclosure attract greater significance. Retaining high standards of disclosure is important for investor engagement but also vital for trading and for a market to be competitive. On the FCA's approach to significant transactions, we believe that investors and the UK market as a whole merit a higher standard for disclosure than is currently proposed by the FCA, and we propose an alternative disclosure model which we believe achieves this.

Regulatory and market guidance are vital for an attractive and effective market

3. It is vital to ensure that high quality regulatory and market guidance will be in place to support participants navigate and comply with the new regime. The time this will take, and its importance must not be underestimated. The extent of change from the existing regime throws up gaps in guidance where issuers and advisers will be in the dark on how to interpret and apply the new rules, and also shines a light on existing guidance that needs to be updated. The intentional flexibility that is built into the new regime also increases that need.
4. The FCA has specified topics of guidance that it intends to issue but it is of concern that the short implementation period will allow for only very limited public consultation and a short window for the market's familiarisation. Moreover, in our view, immediate guidance is needed for
   - the information on how directors have reached a valuation, when required to be disclosed in a significant transaction notification;
   - application of the complex financial history rules under the Prospectus Regulation Rules for prospectuses;
   - interpretation of the disclosure on significant transactions by companies in financial difficulty required under the UKLR7 Annex 2 Part 5, and the definition of "severe financial difficulty";
   - the sponsor's confirmation of a board's "fair and reasonable" statement for related party transactions.
5. We encourage the FCA to consider how the market, including professional bodies, might help with its plans for guidance. For example, ICAEW is willing to assist in the development of complex financial history guidance. In terms of regulatory guidance, it is of concern that the timescale for implementing the UKLR will allow for only limited public consultation and, importantly, familiarisation of the market including for directors, investors and advisers.
6. Market guidance has a longstanding role in supporting the current regime and those responsible for its development recognise the need to review and potentially revise their guidance. ICAEW is aware of the likely need to update its respective guidance materials for preparers of pro forma financial information and preparers of prospective financial information and review the scope of its guidance on financial position and prospect procedures.

Implementation of new rules is a major change

7. The brevity of the proposed implementation period of two weeks (paragraph 1.36) has not been justified in the consultation paper. The process for publishing final regulatory guidance plus the need to allow the market reasonable time to become familiarised with a new regime have not been given sufficient consideration. The short implementation period risks putting undue pressure on companies and their advisers, potentially disrupting deals and possibly damaging the reputation of the UK market, including its reputation for well-thought through regulatory change.
8. For significant transactions, under the transitional provisions, companies will have to "as soon as reasonably practicable after the transition date and prior to completion" produce and enhanced notification for any "mid-flight" Class 1 transactions, unless they have already published a circular. Given the exact timing of when the new rules will come into force, this leaves companies having to prepare for BOTH a circular and an enhanced notification until greater certainty is given on the implementation date for the UKLRs.
9. The FCA should extend the length of implementation to allow companies more time to prepare once the FCA announces the transition date. We recommend an implementation period of 2 to 3 months.

ANSWERS TO SPECIFIC QUESTIONS

Q1: Based on our overall proposals for commercial companies, and taking into account the broader UK regulatory, legal and corporate governance environment, do you believe that we have struck the right balance in designing a proposed regime that enables the conditions for a stronger, more effective and competitive listed market with appropriate measures in place to support market integrity and investor protection. If not, what changes should be made?

10. We believe that the UK market should aspire to a higher standard of disclosure to meet investors' information needs than that in the FCA's proposed disclosure regime for significant transactions. The proposed timing and content of disclosures are an inadequate replacement of shareholder votes and related circulars, and the regime falls short of ensuring both an issuer's accountability to its investors and investors' ability to engage with an issuer, regarding the merits of a transaction.
11. We recommend changes to address this in our response to Q8.

Q8: Do you agree with our proposed enhanced disclosures regime for significant transactions? If you disagree, what changes do you consider we should make and why?

12. In developing the proposed regime for significant transactions the FCA has made welcome changes to the approach in the previous consultation paper[1]. However the obligation in UKLR 7.3.1R2(b) on the issuer to include "any other relevant circumstances or information necessary to provide an understanding of, and to enable the shareholders to assess, the terms of the transaction and its impact on the listed company", will be challenging to fulfil with confidence absent more detailed disclosure requirements or minimum standard of what to include. In contrast, EU Prospectus Regulation and the UK regulation both set out accounting frameworks that are deemed equivalent to IFRS and meet a baseline for financial information disclosure in a prospectus. In our view, this FCA reform is not progressive. It will permit use of accounting frameworks that differ from IFRS and/or ones that investors may not be familiar with. For UK investors/potential investors, in particular, this is at odds with the overarching government policy of encouraging more equity ownership.

[1] CP23/10: Primary Markets Effectiveness Review – Feedback to DP22/2 and proposed equity listing rule reforms | FCA

13. Consistency is also threatened through introducing flexibility to the basis of preparation of pro forma financial statements. This should be mitigated through regulatory guidance or updated market guidance such as ICAEW's guidance in this area.
14. We believe that improvements to the disclosure regime are needed to mitigate the risks of information asymmetry and loss of consistency. The absence of a sponsor role or independent vetting of the significant transaction notification by the FCA results in companies being left to navigate whether or not they have met the FCA's interpretation of any additional "information necessary" to inform investors. We recommend that clear guidance is produced by the FCA on this UKLR requirement.
15. A higher standard for meeting investor information needs than currently proposed by the FCA, will also encourage better governance over disclosures, and boost the effectiveness of stewardship.
16. ICAEW's view of what a higher standard of disclosure would look like is presented as an alternative model in the Appendix, together with explanatory commentary.
17. In developing the alternative model we have carefully considered the FCA's commentary included in CP23/31 on what market participants find causes friction, and insights from our members and other market participants with whom we have exchanged views. We have identified additional areas where FCA guidance is needed (paragraph 4) and we also recognise that there may be a need to update ICAEW market guidance to help support preparers of information included in the alternative model.
18. The FCA's proposed disclosure of financial information in the announcement will make notification harder for issuers than it is under the current LR as it introduces friction at the point of announcement, ie earlier than a circular would be produced. In contrast, our model provides for additional post-announcement disclosures, avoiding friction at announcement and completion, to ensure investors are appropriately informed of an issuer's business and prospects. Similar to the proposals in CP23/31, our model provides issuers with sufficient flexibility to execute significant transactions and does not require the FCA to review and approve the disclosures. It will not add unnecessary regulatory burden on issuers or delay to the overall M&A timetable.
19. Our model also does not diverge from the FCA's requirement that an issuer appoint a sponsor only when it seeks individual guidance in relation to a significant transaction or requests an FCA waiver or modification of the UKLR requirements for significant transactions, including on the class tests. However, as noted in our response to Q11, there is need for more clarity from the FCA on what constitutes a sponsor service.
20. We are ready to discuss this with the FCA and other market participants who have expressed their interest in considering our model.

Q11: Do you agree with our proposed approach to when companies should be required to appoint a sponsor on significant transactions (ie, limited to where issuers apply to the FCA to seek individual guidance, waivers or modifications)?

21. Without disagreeing with the proposed approach, we observe that where a sponsor is engaged to assist with UKLR interpretation and/or request an FCA waiver or modification, there would appear to be a disconnect with the sponsor not having to review the transaction announcement notification, despite interacting with the FCA on the transaction. This removes the sponsor's ability to ensure that the facts presented in obtaining such guidance/waiver have not been amended such that the guidance/waiver may no longer be applicable.
22. We highlight that, in practice, most issuers will have a corporate broker (which itself is likely to be a sponsor firm and may be involved in the transaction as the financial adviser) and will usually receive/review announcements as part of their retained role. In such circumstances,

we would expect the sponsor firm to comment on any UKLR requirements. Should the FCA not mandate a specific sponsor review of the transaction announcement, in particular to ensure UKLR compliance, there is likely to be further disconnect between a sponsor's record-keeping obligations and what does and does not constitute a sponsor service? In certain instances, they have some involvement in a transaction but there is the absence of their required approval. Clarity on the perimeter of a sponsor's obligation would be important.

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APPENDIX

ALTERNATIVE MODEL TO THE PROPOSED ENHANCED DISCLOSURES REGIME FOR SIGNIFICANT TRANSACTIONS IN CP 23/31

Proposals	Explanatory notes
Disclosure model We propose the following as a minimum disclosure regime for significant transactions:	The alternative model maintains the position under the current LR, whereby the transaction announcement contains a minimum amount of transaction-critical information (LR 10.4.1R) and hence does not, in itself, act as a barrier to entering into/announcing the transaction to the market. The alternative model departs from the FCA's model by proposing additional announcements at completion and (up to) 90 days after completion, which, in total, results in a disclosure level that is more substantial than the FCA's model, but also lighter than the current Class 1 regime. The requirements for each of these announcements would be tailored to provide increasing amounts of information when the issuer ought to reasonably be in a position to provide such information without significantly affecting the timetable for the transaction. These announcements would not be applicable for transactions where a prospectus is required, on the basis that the prospectus would contain at least the same level of disclosure as these announcements (which assumes, in part, that the current prospectus requirements are maintained, and complex financial history requirements are clarified).
► **Transaction announcement:** the listed company must notify the market as soon as possible after the terms of a significant transaction are agreed – with that disclosure being:	We have concerns that the FCA's model, through the proposed additions to the transaction announcement above the current Class 2 notification requirements (LR 10.4.1R), will create significant tension between the requirement to include this substantially increased disclosure in the announcement (and hence time needed to prepare this information) and the requirement (under MAR, as well as commercially) to

Proposals	Explanatory notes
	announce the transaction in a timely manner.
• As the FCA propose in UKLR 7 Annex 2 Part 1 (Information relating to the transaction)	This requirement is per the FCA model (and closely aligned to the current Class 2 notification requirements)
• (Acquisition only) As the FCA propose in UKLR 7 Annex 2 Part 4.1 (Synergy benefits)	This requirement is per the FCA model
• (Acquisition only) Profit forecast and profit estimate disclosures, in accordance with requirements as currently set out in LR 13.5.32R - 33BG with respect to profit forecasts or estimates made on the target or enlarged/remaining group.	Where profit forecasts exist on the target, or enlarged group, appropriate disclosure of the basis for the existing forecast would be appropriate.
► **Completion announcement:** at the point of completion, the listed company must notify the market with the following disclosures. This separate completion announcement would not be separately required where the transaction requires the publication of a subsequent prospectus (which would include at least this level of information). Disclosure:	One of the more fundamental investor protections that the current Class 1 circular regime provides is comfort that the enlarged group (for an acquisition) or remaining group (for a disposal) continues to be a going concern, through the requirement for a working capital statement to be made by directors in the circular. We propose that this requirement is maintained but in a modified form that is responsive to the desire for listed companies to be able to complete transactions more quickly, but still provides a significant degree of comfort to investors. At the point of completion, where the listed company announces completion, they would make a ‘going concern statement’ on a negative confirmation basis.
• Confirmation that completion has occurred;	
• Either ▪ Any updates to the required content of the transaction announcement as a result of material changes to facts	

Proposals	Explanatory notes
and circumstances since the announcement; or ▪ Confirmation that the content of the transaction announcement remains valid and complete – ie, a "continuing validity" statement.	
• (Acquisition only) The anticipated date at which further information on the target will be provided;	
• (Disposal only) As the FCA proposes in UKLR 7 Annex 2 Part 2 item 2.3 (Disposals) sub-items (2), (3), (4) and (5)1 (Information relating to the transaction)	The FCA proposal, in UKLR 7 Annex 2 Part 2 item 2.3 (Disposals) sub-item (1) for audited consolidated financial information covering the target (i.e. the disposal business) is more onerous than the current LR requirements. Given the proposed required disclosure of an unaudited financial information table covering the disposal business (sub item (2)) (and mirroring the current LR requirement), the proposed audited financial information would add little benefit.
• Enlarged group/remaining group going concern statement on a negative confirmation basis, assuming the transaction has occurred. ie, "the Directors have specifically considered the impact of the transaction on the Group's going concern position and have no reason to believe that the directors will not be able to adopt the going concern basis of accounting in the consolidated financial statements of the Group covering at least 12 months from date of this announcement". This disclosure would set out the basis upon which the Directors have assessed the Group's going concern position to make the required confirmation; and	The negative form of the statement is a response to the likely shorter period of time between Sale & Purchase Agreement (SPA) signing and completion date and the potentially limited access that the listed company will have to the target in this period, where the transaction is an acquisition. However, the principle remains that the Directors should robustly assess the solvency/liquidity of the enlarged group for the 12-month period to support the statement. This would require specific guidance from the FCA potentially considering sources such as the Financial Reporting Council's 'Thematic Review: Viability and Going Concern' which focuses on "clear and comprehensive viability and going concern disclosures". ICAEW's guidance on prospective financial information (TECH 04/20CFF) could be updated to provide a framework for this statement.

Proposals	Explanatory notes
• A statement by the Directors of the listed company confirming that completion of the transaction will not adversely impact its continuing ability to comply with the Listing Principles.	We note the proposal from the FCA to include a ‘Director’s confirmation’ of a similar form at the point of IPO, and the existing sponsor requirement to make a similar declaration at the point of a Class 1 transaction. It would seem logical for the alternative model to have a similar Director’s confirmation at the point of the completion announcement and make it a public statement so that investors are clear that the Directors have made this assessment.
► **’90-day’ document** (Acquisition only): following completion of the significant transaction, in the period up to a maximum 90 days after completion, more detailed disclosure is provided, as set out below. This 90-day document would not be separately required where the transaction requires the publication of a subsequent prospectus (which would include at least this level of information). Disclosure:	This proposal is not dissimilar to the US Rule 3-05 requirement, under which further disclosures are filed on Form 8-K, in connection with a substantial acquisition, up to 75 days after completion of the transaction. This document would be focussed on providing sufficient disclosure for investors to understand the target business including new risks/changed risks associated with the new business and plans to address/mitigate these, assurance over the recent track record of that business to help set out the potential impact on the listed companies business, and details of any material contracts, litigation and related party transactions. To avoid duplication between different regimes (and assuming that there will be no significant change to the current complex financial history rules when the UK Prospectus regime is revised), where the listed company needs to publish a prospectus in connection with the transaction (for admission of shares to trading on regulated market) this ’90-day’ document would not be required. The 90-day limit could be subject to FCA derogation, for example, where the target was a significant carve out, the period may be extended by the FCA.
• Either ▪ Any (further) updates to the required content of the transaction announcement as a result of	

Proposals	Explanatory notes
material changes in the Directors' understanding of the acquired business having taken control of it; or ▪ Confirmation that the transaction announcement remains valid and complete – ie, a "continuing validity statement".	
• Details of new risk factors or changes to the listed company's material risk factors as a result of the transaction with discussion on how directors of the listed company plan to address/mitigate the identified risks;	
• Two years of audited financial statements of the target required dependent with those financial statements able to be prepared in accordance with • UK adopted IAS; • any equivalent GAAP determined as such under equivalence decisions (eg, US GAAP etc); or • national GAAP of the target, subject to the following provisions: o Prepared on a consolidated basis (where the target is a group) o Contains ▪ balance sheet ▪ income statement ▪ cash flow statement ▪ accounting policies and explanatory notes. o a prominent statement that the target's financial statements included in the document has not been prepared on the same basis as the listed company's latest financial	The two year requirement for audited financial statements is consistent with the FCA's model. The provision of a range of accounting frameworks provides flexibility: - should the target have financial statements readily available in their national GAAP or a widely accepted GAAP. - Should the preparation of the financial statements be complex (for example, carve out financial statements prepared at a perimeter for which financial information has never been prepared) the acquirer may determine it appropriate to align accounting framework/policies with its own in the included financial statements. - Where the acquirer believes that inclusion of readily available financial statements would not be appropriate (perhaps due to significant accounting framework or policy differences), they could opt to prepare the financial statements under aligned accounting framework/policies. In any event, where the financial statements are not aligned with the

Proposals	Explanatory notes
statements and that there may be material differences in the financial information had the listed company's accounting framework and policies been applied in the financial statements;	accounting framework/policies of the acquirer, one year would be aligned for pro forma purposes (see below).
• Pro forma financial information ▪ Prepared in accordance with current PR Annex 20, sections 1 and 2 only ▪ Therefore, no accountant/auditor report required on pro forma financial information	We would seek to retain current pro forma preparation requirements to ensure that the basis of preparation is robust, and consistent with current market practice and requirements that apply to prospectuses. Accounting framework/policy differences between the target's financial statements (as included in the document) and the listed company's latest financial statements, would be reconciled within the pro forma (albeit for a single year), so that the target's financial information can be combined with that of the listed company on a consistent basis.
• Significant change statement on the target;	As per FCA model
• Disclosure of material legal and arbitration proceedings of the target (at date of the document);	As per FCA model
• Disclosure of material contracts of the target (at date of the document); and	As per FCA model
• Disclosure of any related party transactions made by the target in the previous 12 months.	As per FCA model

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