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UK Regulation post-Brexit

Adjusting to the landscape for UK equity capital market participants

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With the EU and the UK having reached a free trade agreement which sets out a framework for the substantial agreements to be put in place to govern their future relationship and the UK having left the single market and the customs union, considerations may turn to changes relevant to admissions or offerings. The "Trade and Co-operation Agreement" sets out the thinnest of arrangements for trade in financial services (see overview here).The TCA has no tangible impact on the rules relating to offerings or admissions to trading of shares, in the UK, or the continuing obligations of UK listed companies. Even so, the end of the transition period did not result in a UK legislative or regulatory vacuum. The European Union (Withdrawal) Act 2018, as amended by the European Union (Withdrawal Agreement) Act 2020 (WAA), ensured a functioning UK statute book outside of the UK's membership of the EU by "onshoring" EU law as it applied in the UK at the end of the transition period, on 31 December 2020.

This means the UK has its own versions of the EU market abuse, transparency and prospectus regimes, among others. These mirror the EU regimes, with differences limited to those required to create standalone UK regimes to reflect the UK's status outside the EU. To achieve this, the UK Government made statutory instruments to adapt the onshored regime, including removing references to EU reciprocal arrangements and institutions, such as prospectus passporting rights. This body of UK law is known as "retained EU law".

The differences required to untangle the UK regimes from their EU counterparts have some practical implications for UK listed companies and other equity capital markets participants. This publication provides a snapshot of these implications for admissions, offerings and continuing obligations. It also briefly explores emerging areas of future divergence between the EU and UK financial services regulatory regimes.

The onshored UK market abuse regime

Many of the core provisions of the UK Market Abuse Regulation (UK MAR) applicable to issuers of shares remain the same as those set out in the Market Abuse Regulation EU 596/2014 (EU MAR).UK MAR retains broadly the same scope as EU MAR, of conduct with respect to financial instruments admitted to trading or traded on UK and EU trading venues. This captures shares admitted to UK or EU regulated markets or MTFs. Even so, we note that:

– While the same exemptions are available for issuers undertaking share buybacks or stabilisation, duplicate reporting requirements to EU national competent authorities and the Financial Conduct Authority (FCA) may arise. ESMA and the FCA have acknowledged that share buyback activity on EU trading venues will potentially be within the scope of both EU MAR and UK MAR. ESMA's review of EU MAR discusses the fact that share buyback activity could potentially need to be reported to several European national competent authorities where the shares are admitted to trading on their markets. Where a share is admitted to trading on a UK trading venue, the FCA has stated it also expects such activity to be reported to them (see FCA Primary Market Bulletin no. 32 here).

– There are no UK policy changes, in the onshored UK requirements relating to market soundings, insider lists, or to the prohibitions on unlawful disclosure of inside information, insider dealing and market manipulation. However, EU policy changes are under consideration by the European Commission.

– The content and format of PDMR transaction notifications remain the same, in the UK and EU, at January 2021, albeit UK changes to the timeline for the reporting of such notifications are expected later in 2021.

– The FCA's intention is to ensure it retains the ability to sanction and investigate cases of market abuse related to financial instruments that affect the integrity of UK markets. It remains to be seen whether the UK will take any action with respect to conduct on any EU market.

Future changes to the UK and EU market abuse regimes

UK

The UK's draft Financial Services Bill is the first move by the UK Government to craft a UK financial services regulatory model separate from the EU regime. The Bill has received its second reading in Parliament. It would bring a welcome change to the UK PDMR dealing notification period, allowing issuers two business days from receipt of the notification of the dealing to announce it to the market. There would also be a clarification that an issuer and persons acting on its behalf must maintain an insider list when in possession of inside information.

EU

We expect there will be some changes to the EU MAR regime as a result of the review of EU MAR that is taking place. This is the first of the periodic reviews that are hardwired into EU MAR. It is premature to comment as the Commission is considering ESMA's proposals. We propose to comment in a future publication in this series.

Updating UK listed company systems and controls to reflect UK MAR

It is advisable to consider updating MAR policies and procedures – and related training – to reflect the changes in law that took effect at the end of the transition period, given the importance the FCA attaches to these as part of an issuer's Listing Principle 1 compliance. As well as updating statutory references in policies and other documentation, and monitoring the impact of future divergence between the EU and UK regimes, UK issuers of shares will note the potential impact of extra FCA scrutiny regarding use of the mechanism which permits delay in disclosure of inside information. A detailed notification has to be submitted to the FCA at the same time as the inside information is announced to the market, under UK MAR Article 17(4). This increased oversight follows a review into the use by UK issuers of the mechanism, which the FCA published in Primary Market Bulletin no. 31.

The FCA has identified two main areas of focus for this additional scrutiny of use of the delay mechanism.

– Unscheduled financial information, such as trading updates and profit forecasts: as it is more challenging to find a legitimate basis to delay this type of financial information than scheduled financial information.

– Director or other board changes: as ESMA's (non-exhaustive) guidance, which remains applicable in the UK, does not identify these developments as a legitimate basis for use of the delay mechanism.

In addition, UK listed companies will want to take account of an FCA focus on the content and timing of market announcements and ensure they have systems in place to ensure these are accurate and not misleading. It addressed this in a series of utterances in 2020, including in two Final Notices that followed enforcement action.

The "free float" requirement is revised to reflect the UK's status outside the EU

The 25% free float test, that applies to premium listed companies both as an eligibility criterion and a continuing obligation, has been revised to include shares held by the public in any jurisdiction, whether or not listed there.

Separately, to maintain London's competitive position, HM Treasury launched a call for evidence which included a question about whether free float is the optimum mechanism to ensure there is liquidity in an issuer's shares.

The onshored UK transparency regime

The UK Transparency regime preserves the existing EU regime as it applies to issuers in the UK. It was onshored by amendments made to Part VI of the Financial Services and Markets Act 2000 by the Official Listing of Securities, Prospectus and Transparency (Amendment) (EU Exit) Regulations. The operative provisions of the transparency regime in the UK remain set out in the Transparency Rules (DTR 4, 5 and 6) and require the filing, notification and dissemination of "regulated information". Points of note include:

– Pursuant to an equivalence direction, UK issuers can continue to prepare financial statements (for use in prospectuses and annual/interim accounts) in accordance with EU adopted IFRS.

– Issuers who have securities listed or admitted to trading on a regulated market in an EU Member State (and who had chosen the UK as their Home Member State) have until 31 March 2021 to choose a new Home Member State and notify the relevant authority. Otherwise, a default Home Member State will apply, based on the location of admission of their securities to trading on a regulated market in the EU.

– The EU has not given any indication that it will find UK IFRS accounts equivalent to EU adopted IFRS. This is only likely to present a practical challenge if UK and EU adopted IFRS start to diverge.

– UK issuers of securities admitted to trading on a regulated market in the EEA and vice versa will need to comply with the registration requirements for third country auditors in their respective countries. This is unlikely to present issues for UK issuers as the UK is treating EEA states as equivalent for audit purposes.

– The FCA has published an updated version of its list of the third country regimes it considers equivalent to the UK regime for the purposes of DTR 4, 5 and 6 (**here**).

The onshored UK prospectus regime

The framework is set out in the UK Prospectus Regulation and Part VI of the Financial Services and Markets Act 2000. It applies to offers to the public or admissions to trading on a UK regulated market. Considerations include:

– *Loss of prospectus passporting rights:* at the end of the transition period, the ability to passport a prospectus between the UK and EU under the EU Prospectus Regulation EU 2017/1129 (EU Prospectus Regulation) ended. There is a time-limited grandfathering provision. Relevant UK exit regulations provide that prospectuses that were approved by an EU competent authority under the EU Prospectus Regulation and passported into the UK by 31 December 2020 are grandfathered for use in the UK until their validity expires (12 months post-approval). As a result, a prospectus may be treated as approved by the FCA where it received a notification of approval in accordance with the EU Prospectus Regulation by the Relevant State, before the end December 2020 deadline, and used for a UK retail offer, until expiry.

– *Rights issues and open offers:* issuers with an FCA approved prospectus, who wish to undertake a rights issue or open offer and to offer shares to the public in EU27 countries on a non-exempt basis, will need to review the composition of their investor base even more carefully than pre-Brexit to determine the geographical distribution and numbers of EU27 residents. These issuers will either need to obtain approval from an EU27 NCA or exclude shareholders in the relevant EU27 country from the transaction.

– *Exempt offers or admissions may benefit from parallel EU and UK exemptions:* offerings or admissions that are exempt from the EU Prospectus Regulation are eligible to benefit from equivalent mirror exemptions under the UK Prospectus Regulation eg admissions of up to 20% increases of share capital over a rolling 12 month period and offers to qualified investors.

– *Regarding guidance on prospectus content:* UK issuers should continue to have regard to ESMA's 2013 Prospectus Directive Recommendations. The FCA will consult, in due course, on its approach to ESMA's 2020 Prospectus Guidelines which are expected to become applicable in the EU in 2021.

Future changes to the UK and EU prospectus regimes

It is not anticipated that the UK will have a role in formulating, or will implement, EU initiatives arising out of the EU Capital Markets Action plan or the Commission's Recovery Plan. This means, for example, that the UK is unlikely to adopt the alleviated-content EU Recovery Prospectus, unlike the EU27.

"Equivalence"

The UK has the status of a third country with respect to EU law and vice versa.

UK

The UK has granted equivalence to EU law regimes in a number of areas. The equivalence decisions on presentation of historic financial information in a prospectus have been domesticated into the UK and HM Treasury has issued an equivalence decision that EU-adopted IFRS can be used in the UK for prospectus and transparency purposes.

EU

It is unlikely there will be a finding of equivalence by the EU under the mechanism set out in the EU Prospectus Regulation in respect of prospectuses prepared under UK law and approved by the FCA, to those prepared under the EU Prospectus Regulation. This is because ESMA has already stated that the mechanism is not fit for purpose.

References in documentation, including selling restrictions and legends, will need revisiting

Market participants will need to effect UK-related updates to selling restrictions and legends in documentation, including referring to EU retained law measures, and may also need to update the various other statements and references to EU legislation and concepts included in documentation.

– If an issuer has listings or admissions in the UK and EU, it is likely to need to comply with both the UK onshored and UK regimes and to reflect this position in documentation. Otherwise whether the UK onshored regime or the EU regime will apply, will usually be determined by where the issuer is listed or is seeking a listing or where an activity takes place.

– The Association of Financial Markets for Europe (AFME) has prepared revised versions of its selling restrictions, certain legends, product governance materials, its industry-standard Agreement Among Underwriters and block trade agreement and has created a UK version of its contractual recognition of bail-in wording for underwriting documentation, among others.

- Public offer selling restrictions for equity transactions will need to be amended to reflect the end of the transition period (removing references to the "United Kingdom" in the EEA public offer restriction) and adding a mirror UK public offer selling restriction. The UK restriction mirrors the EEA public offer restriction (as the UK law still follows the EU framework at January 2021).
- Product governance legends for use by UK manufacturers will need to be amended to reflect the fact that the UK is not a Member State and has its own UK MiFIR Product Governance requirements set out in the FCA Handbook.
- Banks that prefer to include accidental customer language will need to consider which entity (EEA or UK) will be underwriting and whether a MiFID service or UK MiFIR equivalent is being provided to investors or whether the CFC exemption can apply.

Status of EU guidance in the UK

The FCA has recognised the value of existing ESMA Level 3 material (such as guidelines, recommendations and Q&A) and has decided that it will continue to apply in the UK, to the extent relevant to the UK's positon outside the EU, interpreting it sensibly and purposively taking into account the UK's withdrawal. For example, ESMA's guidance regarding risk factors and APMs has been carried forward.

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