

Implications of the new Listing Rules on the sponsor regime

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Introduction

On 29 July 2024, the new Listing Rules came into force (**new UKLR**), as part of the biggest overhaul of the regulatory framework for listed companies in over three decades. This briefing focuses on the changes made to the sponsor regime.

Retention and scope of the sponsor regime

The FCA's Primary Market Effectiveness Review, which began in 2021, included a fundamental review of the sponsor regime, with the FCA questioning whether the regime should be kept at all.

In recognition of the reliance the FCA places on sponsors in assisting it in exercising its functions, the sponsor regime has been retained, although the scope of the sponsor role has been modified. Sponsors will continue to play a crucial role in ensuring compliance with the new UKLR, particularly for issuers in the new Equity Shares in Commercial Companies category, closed-ended investment funds, and shell companies.

A sponsor is still required on an IPO to assess and provide assurances to the FCA that the applicant has met the listing and prospectus requirements. However, the sponsor's post-IPO role has been reduced as there are now fewer instances where an issuer is required to engage a sponsor.

Specific circumstances requiring a sponsor

Issuers must engage a sponsor in the following circumstances:

- transactions involving the publication of a prospectus (e.g. on an IPO or a secondary fundraise involving the issue of more than 20% of the issuer's listed share capital);
- when a "fair and reasonable opinion" is required on any large related party transaction (being one that exceeds 5% in any of the applicable class tests) or (in the case of a closed-ended investment fund) any relevant related party transaction (being one that exceeds 0.25% in any of the applicable class tests and which relates to the investment manager's fee or other remuneration);
- when seeking individual guidance from the FCA on the application or interpretation of the new UKLR or modifications or waivers to the new UKLR, such as a waiver or modification of the significant transactions regime, including the class tests, or the related party transactions regime;
- transactions involving the submission to the FCA of a reverse takeover circular or (in the case of a closed-ended investment fund) a circular relating to the approval of a relevant related party transaction (being one that exceeds 5% in any of the applicable class tests and which relates to the investment manager's fee or other remuneration); and
- transfers of an issuer's listing category.

Sponsor's declaration

A sponsor declaration to the FCA continues to be mandatory on IPO, as well as on the transactions referred to above which involve the publication of a circular or prospectus and transfers between listing categories.

The content of the sponsor declaration remains broadly similar to the requirements under the old Listing Rules but sponsors should ensure that they download the latest (updated) forms from the FCA's website.

Sponsor competency requirements

The FCA confirmed that the rules made in **April 2024** to amend the sponsor competency requirements have been carried over into equivalent provisions in the new UKLR. Broadly, these changes allow sponsors to demonstrate competence relying on transactions requiring a sponsor's declaration from within the previous five years (instead of the last three years).

If sponsors cannot satisfy the above, they can demonstrate competence through experience gained from providing certain corporate finance advisory services in the previous five years with issuers admitted on a UK recognised investment exchange (e.g. AIM or Aquis) and with a minimum market capitalisation of, in the case of commercial companies, £30 million. The types of services include acting as an IPO adviser on AIM or Aquis, acting as a sponsor on services not requiring a declaration (e.g. a fair and reasonable opinion on a related party transaction) and acting as an adviser on a public company takeover.

Technical notes

The FCA has been adopting a phased approach to consulting and updating its technical notes in its Knowledge Base which support the Listing Rules.

Primary Market Bulletin No. 48 (PMB 48)

On 26 April 2024, the FCA published **PMB 48**, which consulted on:

- one new technical note (**TN/721.1**) on the sponsor's confirmation in relation to the modified transfer of listing category regime. The aim is to help sponsors understand the FCA's expectations in relation to the work sponsors must perform when providing the confirmation proposed in a modified transfer scenario, as the form of assurance differs from that typically provided by sponsors in other scenarios; and
- amendments to 13 existing technical notes on the sponsor regime to reflect the changed rule references in the new UKLR.

The consultation closed on 26 May 2024 and the updated/new technical notes are expected to be published shortly.

In PMB 48, the FCA also published final versions of the following technical notes to reflect the changes to the sponsor competency requirements referred to above: **Sponsor transactions - Adequacy of resourcing (TN/709.3)**; **Sponsors: Guidance on the competence requirements set out under LR 8.6.7R(2)(b) (TN/714.3)**; and **Sponsors: Practical implications of competence requirements for sponsors and applicants (TN/715.2)**.

Primary Market Bulletin No. 50 (PMB 50)

On 11 July 2024, the FCA published **PMB 50**, which focuses on the sponsor regime and responds to

feedback from sponsor firms during the FCA's consultations on the new UKLR on aspects of the regime which were considered to be inefficient and/or problematic for sponsors.

The FCA consulted on:

- two new technical notes relating to (i) the FCA's expectations of a sponsor in relation to specialist due diligence and (ii) the supervisory reviews of sponsor firms; and
- an update to an existing technical note on sponsor record keeping.

The consultation closed on 5 September 2024 and the updated/new technical notes are expected to be published later this year.

Specialist due diligence

In response to concerns relating to the sponsor's role in coordinating due diligence in specialist areas, proposed new technical note, **TN/722.1 - Responsibilities of a sponsor: specialist due diligence**, provides guidance on what the FCA regards as its reasonable expectations. The FCA expects a sponsor to apply the Listing Rules, Prospectus Regulation Rules, Disclosure Guidance and Transparency Rules with skill and expertise in the specific context of an issuer's business and operations. However, the FCA does not expect sponsors to be experts in every specialist discipline. Further, the FCA expects sponsors to exercise common sense judgement as corporate finance professionals when determining the level of due diligence proportionate to undertaking the sponsor role with due care and skill and providing opinions after due and careful enquiry. Common sense in this context means applying the judgement possessed by a reasonable professional with skill and experience in corporate finance, after assessing information carefully, with curiosity and a sceptical mindset.

The FCA emphasises that it is within the judgement of a sponsor to determine when specialist reporting by a third party is appropriate. The FCA does not expect to see third party reports where a sponsor is able to reach its opinion without such a report.

The FCA also notes that, in addition to customary reports by specialists such as minerals experts and property valuers, it is increasingly seeing sponsors involve other experts such as environmental and climate reporting specialists.

The FCA highlights that a sponsor cannot delegate its obligations as sponsor to a third party or rely on the assurances of an expert without due care and enquiry. The FCA would expect the sponsor to consider the capacity and capability of the expert; review and approve the scope of work; review and comment on, or challenge, the draft and final reports; discuss the report with the issuer's board, where relevant; and consider if any bring down process is necessary if there is a gap between the date of the report and the date on which the sponsor gives its declaration to the FCA.

The FCA expects a sponsor to keep a record of the considerations referred to above, including, for example, copies of engagement letters, key correspondence with the expert or in relation to the expert's work, drafts and final reports, and notes of meetings or calls in which the sponsor has questioned or discussed the expert's work. However, sponsors will need to exercise judgement so that they keep material records that serve to demonstrate that they have worked with the requisite level of care, whilst not necessarily keeping records of everything. For example, if a sponsor receives draft and final reports from the expert in line with the scope and they do not reveal matters warranting further discussion or challenge, a brief contemporaneous note of these judgements and the basis of them will be sufficient. In considering what evidence to retain, sponsors should consider the need to demonstrate how they reached a conclusion following a review of any due diligence reports.

Record keeping

In response to concerns about record keeping, the FCA proposes to update technical note, **TN/717.1 - Sponsors: Record Keeping Requirements**, with the inclusion of an appendix containing frequently asked questions and answers.

The FCA expects to supplement the appendix with further questions and answers, drawing on real life examples, as it completes further sponsor reviews.

Significantly, the FCA has amended its guidance in the new UKLR to limit the records required to be kept by a sponsor. Previously, the FCA considered that records should allow a person with no knowledge of the actual sponsor service undertaken to understand and verify the basis upon which material judgments have been made throughout the provision of the sponsor service. The new UKLR 24.4.27G amends this so that the standard is whether a person with a basic understanding of the transaction would be able to understand and verify the basis of such judgements being made.

Issuer understanding of the sponsor's role and obligations

The FCA received feedback which suggests the role of the sponsor is not always well understood by issuers, which may create problems when the sponsor requires additional reporting or documentation as part of its due diligence.

The FCA emphasises issuers must understand the sponsor has important responsibilities to the FCA, and issuers must cooperate with their sponsor. The FCA proposes to write to issuers at the start of an IPO to explain its expectations on their interactions with their sponsor. In particular, the FCA expects to clarify that the sponsor is assisting the FCA in carrying out its functions and that sponsors are closely supervised, highlighting that a sponsor must be able to demonstrate, through its own records, that it has exercised due care and skill and provided opinions after due and careful enquiry.

FCA supervisory reviews of sponsor services

During the FCA's review, some sponsors raised concerns that the FCA's approach to supervisory reviews had led to a disproportionate increase in the work required by sponsors, leading to the implementation of overly burdensome controls in record keeping.

In addition to the updated technical note on record keeping (see above), the FCA proposes a new technical note, **TN/723.1 - FCA reviews of sponsor services**, which explains the FCA's approach to supervisory reviews of sponsor services. The new guidance explains why and how the FCA performs reviews, as well as its approach to providing feedback and what the FCA expects in response.

Amendments to sponsor declaration

Following feedback that sponsor staff members felt individual responsibility when signing a sponsor declaration, the FCA has amended the sponsor declaration forms (available on the FCA's website) to clarify that the declaration is provided by the sponsor firm, not by an individual.

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