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New Rules for Listing on the London Stock Exchange Could Ease the Path to IPO

New stock exchange rules could ease the path for companies to go public earlier in their stage of development. We outline what firms need to know about the rules and the potential implications for the IPO market in London.

The Financial Conduct Authority, a financial regulatory body in the United Kingdom (UK), recently announced changes to the UK Listing Rules, which went into effect on December 3, 2021. The rules apply to companies listed on the main market of the London Stock Exchange.

The rules make three primary changes to the structure and requirements of LSE-listed companies, including:

1. Companies listing on the premium segment can now operate a limited dual class structure for a period of five years from first listing;
2. A reduction in the free float requirement from 25% to 10%; and
3. An increase in the minimum market capitalisation requirement from £700,000 to £30 million.

In this alert, we'll dive into each of these three changes and what companies need to think about as they plan for an IPO.

Dual Class Share Structure

For a period of five years from listing as a "premium-listed company," a company is permitted to operate a different class of shares to allow enhanced voting rights (up to a 20:1 enhancement). This pertains to voting matters related to the removal of a director or on any matter after a change of control. Enhancement does not apply to voting on other matters such as remuneration policy. Therefore, in terms of hot button governance issues like executive compensation, these changes will have a limited impact on the level and structure of pay that companies can adopt post-listing.

These enhanced voting right shares can only be held by a director (or on their death by their estate), and the class of shares must be in existence at the time of listing. The five-year time limit cannot be extended, and it is not possible to refresh the five-year period by undertaking a reorganisation (e.g., placing a new holding company on top of the original listed company).

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This change may be particularly attractive to innovative, high-growth companies where founders may feel more vulnerable to a takeover in the early stages of the company's development. This change also could allow private companies to go public at an earlier stage in their development. This is attractive to shareholders and employees since it creates more opportunity for shareholders to participate in the growth a company's value from an earlier stage and provides liquidity for any stock awards held by employees.

Free Float Requirement

The free float requirement reflects the percentage of a company's share capital that is required to be in public hands (i.e., freely tradeable) at the time of admission and on an ongoing basis. The new rules reduce the free float requirement from 25% to 10%. This new minimum is not meant to be a target, and the FCA does not expect that companies will look to 10% as being the goal for listings going forward. However, it does introduce additional flexibility, which also may encourage more companies to go public.

Minimum Market Capitalisation

The minimum market capitalisation for companies in both the standard and premium segments of the main market has increased from £700,000 to £30 million. The FCA has said that the intention of this change is to give greater clarity and trust to investors with respect to the types of company on the main market. The expectation is that companies with a minimum market capitalisation of less than £30 million would be better suited to the Alternative Investment Market.

Next Steps

Between 2015 and 2020 only 5% of global IPOs took place in London, according to the UK Listing Review. The additional flexibility that these new rules provide, particularly around the dual class share structure, should at the very least give some pre-IPO companies further cause to look at the LSE as a viable option.

These changes also encourage companies to come to market more quickly than in the past. This is likely to place a greater emphasis on company boards and remuneration committees when designing and implementing pre-IPO and post-IPO executive pay arrangements that seek to allow a meaningful share in the growth in company valuations, as well as ensuring that, once listed, executive teams continue to have their interests aligned with new incoming investors.

To speak with one of our experts about this topic or how we help companies transition from private to public, please write to humancapital@aon.com.

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