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Response to Consultation DP16/3 – Availability of Information in the UK Equity IPO process

The CFA Society of the UK (CFA UK) represents about 12,000 investment professionals working across the financial sector including portfolio managers, buy-side analysts, sell-side analysts and credit rating analysts, among others. Our mission is to educate investment professionals, to promote high ethical and professional standards and to explain the profession to our stakeholders. For advocacy purposes, our members are represented by several committees including the Market Integrity and Professionalism Committee and the Financial Reporting and Analysis Committee. Given that consultation DP16/3 deals with both market integrity and financial reporting matters these two committees have provided a joint response on behalf of CFA UK members. The decision of whether to participate in IPOs is an important part of the investment manager's role and we agree that the current process of information disclosure in UK IPOs is below the standards of some other markets.

Questions on the concerns with the current UK IPO process

Q1: Having regard to the typical UK IPO timetable, do you agree that it is in principle a cause for concern that in most cases a draft prospectus is available two weeks after the ITF and a final prospectus is only available after pricing? Please state reasons.

Yes we agree. We see no reason why the pathfinder/draft prospectus should not be published at the time of the announcement of Intention to Float. Waiting for two weeks does not serve the interests of investors and leaves them no alternative than to review the connected research during the blackout period. Anecdotally we are aware of instances where new information was included in the draft prospectus that had not previously been made available to connected analysts and hence was not taken into account in their pre-blackout reports.

As no new information is likely to emerge during the blackout period we fail to see the rationale for delaying the publication of the draft prospectus. The publication of the final prospectus should be immaterial to investors as this document should be identical to the draft save for the addition of the final pricing.

Q2: Do you have concerns about connected research? If so, please describe those concerns.

We agree with the findings of your market study that institutional investors still find value in connected research despite its positive bias. We also agree that only having access to



connected research in the run up to the book building process is an impediment to balanced decision making and that having access to the draft prospectus and unconnected research during this period would be of benefit to investors.

Q3: What is the basis on which you consider legal liability may attach to the publication of research in close proximity to the publication of an approved prospectus? Please explain, by reference to the current legal framework. It would be helpful if you could consider the question from the perspective of both issuers and research publishers.

Given that we represent the views of the investment management community and not investment banks we do not feel this question is relevant for us to answer. We would observe, however, that two weeks seems an entirely arbitrary period. Furthermore, if banks would like to reduce their legal responsibilities they could refrain from publishing research and simply publish the draft prospectus more promptly instead.

Q4: Do you have any comments on regulatory or other possible drivers of the existing blackout period?

We agree with your assessment that avoiding a conflict of interest is unconnected with the pre IPO blackout period. Research from banks involved in an IPO is understood by institutional investors to be conflicted and they interpret it in that light.

Although we cannot confirm this, it may be that the pre IPO blackout period is a measure to delay the publication of the draft prospectus. This forces investors to rely more heavily on the banks' proprietary research. This may in turn drive the pricing process to an outcome that favours issuers and their advisers over investors.

Q5: What do you think are the main barriers to more unconnected research on IPOs? Do you think fostering the conditions for more unconnected research is a suitable objective to improve further the UK process?

The main barriers are those that you have highlighted in your paper, namely, lack of access to management and lack of access to documentation prior to the final prospectus.

Yes we think unconnected research would be a useful complement to the existing sources of information that investors have on IPOs: connected research and, two weeks later, a draft prospectus.

Q6: Do you agree with the concerns that we have set out in Chapter 3?

Yes we agree with the concerns you have highlighted. We see market integrity as the main concern as the reliance on connected research may lead investors to apply a higher discount rate to UK IPOs than to IPOs in markets with better IPO regulation.

With reference to paragraph 3.22 we do not feel the IPO process is relevant to consumer protection, nor do we see the barriers to unconnected research as a competition issue per se but rather as a market integrity issue.



Questions on the proposed options for reform

Q7: Do you agree with our conclusion that a regulatory intervention is required to achieve reform? If not when and how do you believe a market-led solution could be secured?

Yes we agree that regulatory intervention is required to achieve reform. Investment banks are unlikely to voluntarily change the current status quo as it could potentially undermine their business model.

Q8: Do you support these high level aims for reform of the UK IPO process? If not, please set out concerns and/or alternatives.

We agree with the aims of:

- a) Making the approved prospectus the central document in the IPO process and making it available sooner than is currently the case.
- b) Creating conditions that promote the production of unconnected research prior to the book-building process.

We are less concerned about managing the conflicts of interest of connected research as we believe investors already take these into consideration. Having an alternative to connected research (i.e. an early draft prospectus and unconnected research) is of more importance.

Q9: Do you agree that a ban on (i) all research and (ii) only connected research in the IPO process would not be a suitable option for reform? If not, why not?

A ban on all research would not aid the price discovery process. Unconnected research would be complementary to the draft prospectus for investment managers.

Banning connected, pre-IPO research - as is the practice in the US - would be potentially beneficial as it would provide greater incentives for the production of independent research. This would also require that unconnected analysts were given timely access to information and management. Banning connected pre IPO research would also remove any excuses for delaying the publication of the draft prospectus.

Q10: Do you agree that simultaneous publication does not represent a suitable or practical basis for reformed market practice?

No, we do not agree that simultaneous publication of draft prospectus and connected research is not practical. Assuming that there is still a two week window between the draft prospectus publication and the book building process then there is still sufficient time for unconnected analysts to digest the prospectus and provide their views to investors. While time pressures and lack of access to management would weigh against unconnected research providers their independent judgement would still be valued by investors.

Regarding 4.17 we repeat that if banks feel publication of research at the same time as the prospectus increases their legal liabilities then they should refrain from publishing research. This in turn would increase the demand for unconnected research.

Q11: Do you agree that requiring publication of the registration document component of the prospectus prior to the publication of research would improve the IPO process? If not, why not?



We agree that the draft prospectus (or the registration document) should be the core document for investors to base their investment decision on and that bringing forward the publication of this document would improve the IPO process.

Q12: Do you agree that requiring issuers to open the presentation to analysts to unconnected research analysts would improve the IPO process? If not, why not?

Yes we agree. Moreover, we believe that not only should the presentation be made open to unconnected research analysts from other banks and providers of independent research, but it should also be made open to buy side participants. Investment managers are increasingly relying on in-house research to make investment decisions and this is likely to increase further with the adoption of research unbundling under MIFID II.

Opening the meeting to the buy side would create a logistical challenge for an issuer and its advisers regarding who is allowed to attend the analyst meeting, since the number of attendees cannot be unlimited. The decision of which unconnected sellside analysts and buy-side participants are invited to attend the meeting creates a potential conflict of interest. A potential solution would be to make the meeting available over the Internet by webcast.

Q13: Which of models 1 to 3 do you think would provide the best basis for reformed market practice?

We like the suggestion of publishing the registration document (or draft prospectus) at the time of the Intention to Float announcement to give investors as much time as possible to consider it.

We like the suggestion of opening up the analyst meeting to unconnected sellside analysts but we think the proposal needs to go further in that buy-side representatives should also be allowed to attend either in person or online.

We think that to make best use of the analyst meeting this should take place after the publication of the draft prospectus / registration document. This will allow analysts to prepare questions for management rather than simply absorb a presentation of new material.

As such, model 3 appears the best basis for reform.

The timing could be as follows:

Day 1 - ITF announcement and publication of registration document

Day 2-7 – Publication of initial research by sellside analysts

Day 8 - Presentation to connected and unconnected sellside analysts and buy-side representatives

Day 9-14 - Publication of further research by sellside analysts and pre deal marketing

Day 15-27 - Management roadshow and book-building process

Day 28 - Final prospectus and start of trading



Q14: For each model (1 to 3), please consider

- *Are there any practical issues that we need to consider?*
- *Would it lead to an increase in the length of the IPO process?*
- *Would it create conditions for unconnected research to be produced?*
- *Would it lead to any increase in costs or risks for the issuer, investors or intermediary firms?*

As shown by the suggested timings in our answer to Q13 we do not believe the adoption of model 3 would lead to an increase in the typical 28 day length of the IPO process.

We believe this model would create suitable conditions for unconnected analysts to produce pre IPO research.

We believe the costs of catering for additional participants at a meeting, both in person and online, are minimal.

Q15: Are there any other options you think we should consider?

We think model 3 adequately addresses our main concerns about the timeliness of the draft prospectus and the lack of unconnected research for UK IPOs. As discussed above, we think opening the analyst meeting to buyside participants would be an enhancement to the proposed model.

Q16: Do stakeholders have concerns with how conflicts of interest are managed when investment banks' analysts meet an issuer and/or their advisers as part of premandate IPO pitching process? If so, do stakeholders have suggestions on how this could be improved, for example by firms establishing best practices or clarification of our regulatory expectations in this area?

We think it is very difficult to regulate the conflicts of interest in pitching for IPOs. As your own research has shown (2.23) "corporate finance advisers ... consider that a positive research message conveyed by analysts is one of the main factors when advising the issuer on which banks to appoint to the syndicate". However, as previously mentioned institutional investors are aware of this conflict of interest and bear it in mind when assessing connected bank research.

Q17: Would the models of reforms considered above also be appropriate as the basis for reformed practice in IPOs on non-regulated markets?

We are not aware of any reasons why the suggested reforms could not also be applied to non-regulated markets such as AIM. However, in practice the scope for unconnected research in AIM IPOs is extremely limited by virtue of the typically small trading volumes of these securities.



We trust that these comments are useful and would be pleased to discuss them in person.

Yours sincerely,



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Advisor, Market Integrity and Professionalism Committee
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About CFA UK and CFA Institute

The CFA Society of the UK (CFA UK) represents the interests of more than 10,000 leading members of the UK investment profession. The society, which was founded in 1955, is one of the largest member societies of CFA Institute and is committed to leading the development of the investment profession through the promotion of the highest ethical standards and through the provision of continuing education, advocacy, information and career support on behalf of its members. Most CFA UK members have earned the Chartered Financial Analyst® (CFA®) designation, or are candidates registered in CFA Institute's CFA Program. Both members and candidates attest to adhere to CFA Institute's Code of Ethics and Standards of Professional Conduct.

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