

14 April 2008



London
STOCK EXCHANGE

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Dear Adetutu

Response to FSA DP 08/1 – A Review of the Structure of the Listing Regime

London Stock Exchange Group plc is Europe's leading equities business, with around 50% of the FTSEurofirst 100 index by market capitalisation and the most liquid order book by value and volume traded.

We are unique amongst international exchanges in the choice of routes to market we provide: the Main Market (for Primary and Secondary Listings and GDRs), AIM, the Professional Securities Market (PSM) and the Specialist Fund Market. As a consequence, our markets are attractive to companies from different jurisdictions and at various stages of their development.

The Main Market currently comprises 1,219 Primary Listed companies and 334 Secondary Listed and Depositary Receipt (DR) issuers as well as 14,467 debt securities. The PSM has 34 DRs and 515¹ debt securities. These issuers sought admission to listing either via the UK Listing Authority or passported from another EEA Competent Authority.

The Exchange sits at the centre of a diverse network of market participants: issuers, advisors, investors and others. As stakeholders, the Discussion Paper and its outcome are of crucial importance to both ourselves and this wider network. Consequently, we have discussed its contents with many market practitioners and have encouraged them to engage in the debate.

By focussing on admission to listing, the Discussion Paper largely ignores the other checks and balances the London market provides to potential investors. For example, once admitted to trading (the second stage of the listing process) the Exchange places the issuer's securities on an appropriate trading service. By doing so, securities more appropriate for sophisticated investors are suitably differentiated. For example, Depositary Receipts can only be traded on the

¹ London Stock Exchange, March 2008

International Order Book (IOB), a dedicated trading service. The share prices of IOB securities are disseminated via our international data feed. This is a service for professional investors only and a fraction of our data subscribers choose to take this feed. Our own research indicates that trading by retail investors represented less than 1% of the total IOB trading in 2007. FSA's own Conduct of Business Rules requires firms to ensure that investment recommendations or decisions for their clients are suitable for them, depending on the specific needs and characteristics of the client.

Although we are supportive of clearer and more accurate labelling, we do believe that there is a requirement for better education of market practitioners and commentators. We are very willing to support FSA in its efforts with educational initiatives. We do not believe that mandating changes to the display of trading screens will help to inform investors and market commentators. It is the brokers who use this information and not the wider market. We disagree with FSA's suggestion that issuers will be able to influence more than 200 information service providers to change their technology, given the costs that this would involve.

We are concerned that the impact of FSA's proposals upon the PSM have not been given sufficient consideration and urge FSA to redress this. A number of these proposals will be detrimental to the PSM.

Given the numerous discussions the Exchange and FSA have had on the structure of the listing regime, we are confident that our views are clear to you. However, I have summarised them here again for the purpose of responding to the Discussion Paper. We would, of course, be very willing to discuss any of these points in further detail should that be helpful.

Kind regards

A handwritten signature in black ink that reads "Raquel Hughes". The signature is written in a cursive, flowing style.

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Question 1 - Do you consider that the UK 'super-equivalent' Listing standards should be retained?

Yes, we do. We believe the super-equivalent regime creates standards which issuers across the globe aspire to, and which investors value, because of the additional inherent investor protections.

The removal of the super-equivalent listing regime would reduce the choice of listing routes open to issuers resulting in London becoming a less attractive listing venue for companies. It would also limit the choice open to investors and reduce the investor protections currently enjoyed.

Question 2 - Do you consider that the 'super-equivalent' Listing standards should continue to be set by the FSA or should they be determined by the market (exchanges, trade associations or other independent body)?

We believe the current model works well and consider that FSA is the appropriate body to set, assess and monitor the super-equivalent standards.

Question 3 - Should we allow equity securities to be admitted to the Official List if they are only to be admitted to trading on a MTF operated by an RIE or an investment firm and not on a Regulated Market of an RIE? If so, on what basis?

In our discussions with stakeholders it is clear that there is very little demand for FSA's proposals, with the vast majority of commentators opposed to any change at this stage.

Not only do we believe that the proposal would merely be an exercise of academic purity but it would potentially be very damaging. We share our analysis as to why we reach this conclusion, below.

Currently, to ensure that an issuer's securities are afforded a proper and orderly market, UKLA listing is accompanied by an admission to a market (which need not be a regulated market) operated by an RIE. An RIE is subject to statutory recognition and notification requirements. Investment firm operated MTFs differ significantly from regulated markets in two key respects. First they are run as trading venues but without the same level of protections provided by RIEs as required by FSMA and the RIE Sourcebook. Second, MTFs have a very different role under Financial Services Action Plan (FSAP) and other directives than regulated markets.

The requirements of the Sourcebook range from provisions that the RIE has proper consultation processes and disciplinary procedures to protections against

excessive obligations being imposed on issuers by virtue of the Investment Exchanges and Clearing Houses Act 2006 (the “Balls Act”). RIE status assures parties that there are reasonable rules protecting them. RIE status also involves FSA scrutiny of an RIE’s rulebook, and a significantly higher degree of FSA supervision.

RIEs have statutory immunity² from civil suits in the UK in respect of anything done or omitted in the discharge of its regulatory functions (unless it is shown that the act or omission was in bad faith). The benefit of statutory immunity is that RIEs “will not be held back from fulfilling their regulatory duties through fear of litigation. This should increase confidence in their regulatory function and so increase the usefulness of the facilities they provide”³.

The Balls Act came into force in December 2006 and gave FSA new powers under FSMA to review rules and other regulatory provisions made by RIEs, to prevent RIEs from making regulatory provisions which are excessive. The Act was introduced to safeguard the proportionate risk-based regulatory regime that characterises the UK market. Again, such provisions would not extend to investment firm operated MTFs.

The role of Regulated Markets within FSAP and Other Directives

The “primary market” FSAP directives are hinged upon the concept of a ‘regulated market’, as are other important Company Law Directives and UCITS Directives.

The Prospectus Directive regulates the disclosure requirements and publication of prospectuses. The Transparency Directive regulates the disclosure of financial information and major shareholdings on an on-going basis. Both of these directives apply to any securities admitted to trading on a regulated market, but not to securities admitted (solely) to an MTF⁴.

The Company Reporting Directive inserts a new requirement into the 4th Company Law Directive that will require all companies whose securities are admitted to trading on a regulated market to include a corporate governance statement as a specific section in its annual report.

² Section 291 FSMA

³ HM Treasury consultation: Financial Services and Markets Act: Recognition requirements for Investment Exchanges and Clearing Houses (December 2000) Annex B: Draft Regulatory Impact Assessment.

⁴ Technically, the PD would apply to securities admitted to trading on an MTF if it made an offer of securities to the public, as defined by the Directive. However, admissions to AIM show that the Directive’s exemptions can be used where there is not an accompanying admission to a Regulated Market.

The 8th Directive on Statutory Audit contains certain provisions that are only applicable to companies whose shares are admitted to trading on a regulated market, such as the requirement to have an audit committee. The 8th Directive also imposes certain requirements on third country auditors of third country issuers with securities admitted to trading on a regulated market in the EU (but not admitted solely to an MTF).

The UCITS Directives specify that UCITS-compliant investment funds can only invest up to a maximum of 10% of the fund in transferable securities that are not on an EEA-regulated market. This will mean a contraction of the investor base for companies that are admitted solely to an MTF.

Shares that are admitted to trading on an regulated market are subject to the extensive MiFID regime, including: pan-European trading transparency (both pre- and post-trade) regardless of what, if any, venue an investment firm has traded on; transaction reporting; and information-sharing between competent authorities. This is in contrast to the regulatory framework for MTF shares (unless admitted to a regulated market elsewhere in the EEA).

Pre and post trade transparency

The MTF regime is designed almost exclusively around secondary market trading without contemplating that the investment firms running them would also regulate, and have a contractual relationship with, the issuers admitted to them.

This is illustrated by the fact that, in the secondary market, MiFID imposes detailed trade transparency requirements in respect of *shares admitted to trading on a regulated market*⁵. But there are no requirements in respect of shares admitted to trading solely on an MTF.

Likewise, the MiFID provisions on post trade disclosure by investment firms also only refer to shares that are originally admitted to trading on a regulated market (“Member States shall, at least, require investment firms which, either on own account or on behalf of clients, conclude transactions in shares admitted to trading on a regulated market outside a regulated market or MTF, to make public

⁵ Article 29 (pre-trade transparency requirements for MTFs) and Article 30 (Post-trade transparency for MTFs) of MiFID refer to obligations on investment firms and market operators operating an MTF to “make public current bid and offer prices and the depth of trading interests at these prices which are advertised through their systems in respect of shares admitted to trading on a regulated market” and “make public the price, volume and time of the transactions executed under its systems in respect of shares which are admitted to trading on a regulated market”. (emphasis added)

the volume and price of those transactions and the time at which they were concluded”⁶).

Transaction Reporting

FSA has already extended MiFID transaction reporting requirements beyond transactions in financial instruments admitted to trading on a regulated market to those on *prescribed markets*⁷. However, the application of these broader requirements is limited to FSA authorised firms and branches of incoming EEA firms; the requirements do not apply to overseas firms trading on UK markets from outside the UK.

Information-sharing between competent authorities

MiFID puts in place an information-sharing arrangement between competent authorities with respect to transaction reporting, but only in relation to those instruments that are admitted to trading on a regulated market.

We note FSA’s comments that the obligations imposed by the FSAP directives would need to apply to Listed securities.

Extending FSAP to MTF shares

We think there are two broad issues with FSA’s approach.

First, it calls into question the whole point of having two different types of market – regulated markets and MTFs. The FSAP Directives were designed with this structure for a reason and we believe it was never the policy maker’s intention to allow Listing of *shares* to take place on an MTF.

As well as the examples given above, where transparency requirements and transaction reporting were limited to shares admitted to regulated markets under MiFID, a further illustration can be found in the fact that the Systematic Internalisation provisions within MiFID are directed at shares admitted to trading on regulated markets rather than MTFs (“Member States shall require systematic internalisers in shares to publish a firm quote in those shares admitted to trading on a regulated market for which they are systematic internalisers ...”⁸).

⁶ Article 28 of MiFID.

⁷ SUP 17

⁸ Article 27(1) of MiFID.

Second, whilst we do not agree with FSA's approach on policy grounds (for the reasons stated above); we also believe that there are substantial legal and technical issues with FSA's proposals that should not be underestimated.

It is clear that, if investment firms were allowed to list shares on an MTF it is imperative that FSA apply extra rules on MTF operators to replicate MiFID requirements in all respects (they would require MTF operators to have rules in place that would capture their member firms). However, we believe that FSA needs to apply much more thought if it is to successfully achieve this goal.

FSA could impose appropriate trading transparency rules on firms that are *regulated by FSA*. Likewise, the rules of the MTF could apply MiFID-style post-trade transparency requirements on *their members* trading MTF shares OTC. However, this would not address transparency of trading by firms that were not FSA authorised that conducted OTC trading in other jurisdictions.

In addition, FSA will only receive transaction reports from the firms *it authorises* and, even then, only with respect to their UK-based trading (there will be no transaction reports submitted for trades in MTF shares undertaken by UK firms' EEA branches). Furthermore, an asymmetrical set of rules imposed by FSA will create difficulties with their European counterparts when it comes to the vital areas of information sharing, especially in respect of market abuse investigations using transaction reports.

These are gaps that we believe FSA will struggle to 'plug'.

Conclusion

We believe that this proposal introduces a level of complexity that would only serve to confuse investors. In a scenario where Listed shares can be admitted to investment firm operated MTFs, issuers and investors will be subject to different regulatory frameworks which is likely to result in greater confusion.

We also believe that the proposal undermines the very clear role of regulated markets and MTFs envisaged by FSAP. An FSA-driven redefinition of this split creates policy concerns as well as legal and jurisdictional issues.

We do, however, think that Official Listing should be retained for RIE operated markets, including those that are not regulated markets (such as the PSM), given the uncertainty as to the consequences for institutional investors of withdrawal of that status.

Question 4 - Which of the options described do you consider to be optimal? Please provide the reasons for your chosen option.

We strongly support FSA's objective of clearer labelling, however we believe that Option 1 is a disproportionate response that may adversely affect existing and prospective issuers and investors and damage the UK's competitive position.

We are concerned that Option 1 would leave affected issuers of shares with two choices – either to seek a Primary Listing or be removed from the Official List. The former may not be possible and would lead to considerable cost, whilst the latter would have broad implications relating to the status of the issuer, its credibility, profile and its existing investor base, not least because of investors mandate requirements. Issuers of other securities, such as GDRs, would have only one choice - to seek a listing elsewhere. In addition, the impact on existing constituents of the PSM is not yet apparent. These are important considerations for a regulator whose stated aim is to promote the competitiveness of UK markets.

A number of tax reliefs rely on companies' "Listed" or "unlisted" status. Changing the structure of the regime as outlined in Option 1 may have a significant effect on the existing tax breaks. No fewer than nine different pieces of UK tax legislation currently make reference to a company's status in this way. We have been in contact with the HMRC and it is clear the implications are not fully understood.

We also have been in contact with members of the European Commission's Securities Markets Expert Group, who in a recent report noted a justification for preserving Official Listing (rather than relying on MiFID regulated market protections), as follows:

“many institutions are limited through their investment policies to invest – fully or partially – in other instrument than those that are officially listed. In many cases, such policies are designed by the institution itself but the procedures to make changes to the policy might prove to be very complex for a variety of reasons. In our understanding, there might also be external factors, such as statutory requirements, that put constraints on the ability for certain institutions to amend their policies. To this end, a thorough pan-European analysis would be required if the notion of admission to listing were to be abolished”.

It is worth noting that, even if FSA were to implement this change, under the Prospectus Directive an issuer of equity securities or GDRs could seek admission to a regulated market (described and known as a listed market) in another EU member state, e.g. Luxembourg, attain a “Listed” badge and then passport its prospectus to London for admission to trading on the London Stock

Exchange's Main Market. Not only will this undermine FSA's efforts to provide clearer labelling, such an alternative EU venue may be perceived as having higher standards than those applicable to admission to a regulated market in London.

FSA's influence over terminology used by a wide range of market participants globally is questionable. Further commentary on the use of the term listed as a differentiator is provided under Question 8.

Finally, we believe that the UK regime is uniquely attractive due to the choice inherent in the tiered offering. We believe a move by FSA to only have a single entry point to the Official List, via a Primary Listing, would undermine this unique selling point.

Under Option 2, the tiered structure of the Main Market would be retained and unintended adverse consequences for issuers and investors would thus be avoided. This tiered regime is a key component of the London regime and the flexibility and choice it offers is appreciated and favoured by issuers and investors alike.

FSA is concerned that clarity of the various segments would not be improved; however this could be addressed through clearer, appropriate labelling. Such labelling would ensure that market participants understand the different obligations to which issuers of each type of security are subject.

We are therefore supportive of Option 2 as described but believe this can be enhanced by better labelling coupled with a high-profile education exercise.

Question 5 - What are your views about opening up Secondary Listing for UK incorporated companies

If there was demand for such a route for UK incorporated companies, consideration would need to be given to the appropriate trading platform and whether such securities would be eligible for the FTSE UK series of indices to ensure investors are not further confused and the companies are appropriately flagged and segmented. The creation of another regulated market may cause further confusion at a time when clearer labelling is the most important issue to be resolved.

Question 6 - What are your views on how the provisions we have described above under core requirements should apply to overseas Primary Listed companies?

We believe that the rules should be harmonised wherever possible. We are aware that many overseas companies voluntarily apply these standards, as they wish to appeal to the widest range of investors and seek to be included in the FTSE UK Index series, following the principles set out in FTSE's Nationality Practice Note.

However, we understand that harmonisation may introduce regulatory conflict with some regimes, for example as regards company law in the home jurisdiction. Asking companies to comply with standards which conflict with their national law could deter these potential issuers from choosing London at all. If these circumstances do apply, we would ask FSA to adopt a "comply or explain" approach to these requirements.

Question 7 - Should we require the appointment of a sponsor for a transaction involving the issuance of GDRs? If not, are there any other responses to the significant growth in GDRs that are necessary?

The introduction of a sponsor regime would be super-equivalent to the directives requirements and costly for new and existing issuers of GDRs. We are not in favour of a sponsor regime for GDRs - while it brings clear benefits in markets with a large retail participation, it is excessive and unnecessary for the GDR market.

Any increase in the regulatory requirements applicable to GDRs is likely to lead to GDR issuers seeking to list elsewhere – as FSA notes this market is highly mobile. The uncertainty surrounding the DP and the potential subsequent consultation paper(s) is already a factor in decisions about the location of new listings. Feedback from one of the depositary banks is that Russian companies are now considering listing in Hong Kong rather than London due to the possibility of increased regulatory burden and the loss of the listed label.

Question 8 - Do you have views on the labelling options?

Our views on the two labelling options proposed by FSA are largely covered in response to Question 4, above. We believe Option 2 to be the preferred option as this allows the use of the term listed to apply to Primary Listed, Secondary Listed and GDR issuers.

However, we urge FSA to consider more appropriate labels than "Tier 1 Listing" or "Tier 2 Listing – Directive Minimum requirements" to better reflect the

differences in the Listing Rules which apply. Tier 1 and Tier 2 relate to the labels given in relation to capital adequacy and may cause confusion about certain issuers, such as banks. Thus investors might be misled into believing that an issue which is Tier 1 for regulatory capital purposes is also Tier 1 for the purposes of the super-equivalent regime; or that a bank that is subject to the super-equivalent regime has ceased to be so, because it issues a Tier 2 capital security.

Better descriptors are required and we urge the FSA to give this matter further consideration. “Premium” and “Standard” would be preferable alternatives.

The success of the clearer labelling exercise will be the education of market participants and the willingness of those participants to engage and adopt new terminology. It is not clear what FSA itself is proposing to do to clarify the segments and the associated issuer obligations and FSA should be encouraged to spell out clearly on its website the different listing segments and the existing issuers.

Responsibility for Ticker Symbols

We do not believe that requiring issuers to ensure that information service providers (ISP) insert a ticker next to the issuer's name reflecting its listing status is a sensible or practical proposal. Issuers do not necessarily have relationships with ISPs, so any obligation should be on the ISP but FSA has no jurisdiction over ISPs.

Brokers use the information displayed on the trading screens and not the wider market. It is therefore unlikely that mandating changes to screen content will help to educate investors and market commentators. We disagree with FSA's suggestion that issuers will be able to influence more than 200 information service providers to change their technology, given the costs that this would involve.

The Exchange trades different types of securities on distinct trading services. We differentiate between the types of securities on our trading system through the use of the “short name” and segment and sector codes. For example, the Exchange's TIDM⁹ is LSE, it is in Segment SET1¹⁰ and its Sector is FS10.¹¹

⁹ Tradable instrument display mnemonic - the mnemonic code allocated by the London Stock Exchange and used to identify a tradable instrument.

¹⁰ FTSE 100 security

¹¹ FTSE 100 liquid security