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Channel Islands Stock Exchange: An Unlikely Hot Topic

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Introduction

The Channel Islands Stock Exchange (**CISE**) was established in 1998. Since then, it has grown to a current total market capitalization of £393 billion. During 2016, the CISE saw 502 new listings, equivalent to an increase of 18.7%, compared to an 8% increase in 2015, taking the total number of listings to 2,272 at the end of December 2016.

The increased popularity of the CISE has more than one cause. In this note, we address two: (i) the inapplicability of the EU Market Abuse Regulation 596/2014, commonly referred to as MAR; and (ii) the potential advantages of the listing process compared to the two dominant listing venues for high yield debt, the Luxembourg MTF (**Euro MTF**) and the Irish Global Exchange Market (**GEM**).

The Application of MAR to European Exchanges

The EU Market Abuse Regulation 596/2014, or MAR, became effective on July 3, 2016. As stated in our release of March 24, 2015, (*The New European Market Abuse Rules – Looking Towards 2016 | White & Case LLP International Law Firm, Global Law Practice*), MAR covered all areas previously covered by former market abuse directives, including insider dealing, improper disclosure of inside information, market manipulation, timely disclosure of inside information, insider lists, transactions by Persons Discharging Managerial Responsibilities (PDMRs), suspicious transaction reporting and off-market trades. In stark difference from the past, however, MAR applies its market abuse rules to all exchanges within the European Union, while previous market abuse directives directly applied *only* to EU regulated exchanges (such as the London Stock Exchange, the main market of the Irish Stock Exchange, and the Luxembourg Stock Exchange) and *not* to other exchanges within the European Union (such as the GEM and the Euro MTF).

The application of MAR to all exchanges within the European Union has caused numerous issuers of high yield debt to suddenly reconsider their choice of listing venue. High yield debt is offered and traded privately; the listings are typically made only to satisfy other requirements (such as the so-called “quoted Eurobond” exemption, which exempts issuers from withholding tax on interest paid to noteholders if the securities are listed on a “recognised stock exchange”), rather than to provide a trading platform. As, typically, high yield debt is offered on a “Rule 144A/Reg S basis” (referring to the main exemptions from registration under the U.S. Securities Act of 1933 from which transaction parties benefit), disclosure is prepared on a standard that is intended to be comparable to that required if the debt were registered with the U.S. Securities and Exchange Commission. This is a high standard of disclosure, and issuers of high yield debt with no other listed securities (for example, equity listed on one of the main EU markets, or the NYSE or NASDAQ) have historically sought to list their notes on the European Union exchange which posed the smallest additional compliance burden (most commonly the GEM or the Euro MTF).[1]

MAR will now require high yield issuers with notes listed on EU exchanges to train personnel, to implement monitoring procedures, and to maintain real-time insider lists in order to ensure that they are in compliance with the regulation. Furthermore, the common high yield market practice of issuers publishing ongoing quarterly and annual financial information on websites that were only available to those possessing a password, which could only be obtained by contacting the issuer's investor relations department, is incompatible with obligations under MAR to ensure the public disclosure of inside information.[2]

The CISE is a "recognised stock exchange" for purposes of the so-called "quoted Eurobond" exemption, although it is not subject to MAR. It has therefore become attractive to both potential and existing high yield issuers. Since the effective date of MAR, 12 high yield issuers have listed on the CISE, and others are examining whether it would make sense to switch their listing venues, a change which does not typically require noteholder consent.

Listing Process

Although not before now a choice that the high yield market has taken, listing on the CISE would appear to provide process benefits for issuers, such as short announced turn-around times for review after an initial submission (aiming to comment within 48 hours, while both the Euro MTF and the GEM take at least 3 days to complete the same initial review process, and in practice often more). Although typically high-yield issuances are less sensitive to timing concerns than other issuances (as listings are typically undertaken post-closing—at least before the first interest payment on the notes), this does indicate that the CISE is willing to work on a relatively commercial schedule relative to other regulators.

Moreover, the CISE's disclosure requirements regarding the primary listing document (either a prospectus or listing document) are on paper less stringent than either the Euro MTF or the GEM rules, and the CISE has indicated that it has both a "pragmatic" and "flexible" approach to listings, while maintaining the transparency and standards that benefit the market as a whole. Although this is less important on the initial issuance (as all 144A/Reg S high yield offerings should meet the high standard of a U.S. offering in any case), it may become relevant for other listings that occur after some time has passed after the initial issuance, such as privately placed instruments and listings for tax purposes.

Conclusion

Our expectation is that the number of high yield listings on the CISE will continue to sharply increase. We perceive no benefit to issuers in continuing to list on the Euro MTF or GEM. In contrast, the CISE offers issuers a lighter compliance burden and potentially better execution. Any concerns about the lack of sophistication of the CISE trading platform can be ameliorated by the fact that high yield bonds typically trade over-the-counter and not on the exchange. While it is possible that high yield investors may push in the future for listing on an exchange that is subject to MAR, to date this has not been the case, with the buy-side having treated the CISE with relative ambivalence. Provided that high yield issuers continue to act responsibly in terms of their disclosure requirements (including avoiding the use of password protected websites), we expect that this will continue to be the case.

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[1] This is not to argue that issuers are looking to have no ongoing compliance obligations whatsoever. It is standard in European high yield to require issuers to comply with ongoing reporting obligations that track a version of what would be required if they were so-called "foreign private issuers" registering with the SEC (including preparing quarterly and annual reports and requiring the reporting of material events on a current basis to noteholders) and most issuers (whether or not required to do so by the covenants) are in the practice of holding investor calls at the time of their quarterly and annual results.

[2] While both the GEM and the Euro MTF had their own rules that incorporated some market abuse concepts (such as the requirement to timely disclose material information to the market), these were not interpreted by the exchanges or the market to require ongoing information needed to be made public, so long as investors could obtain passwords to the information. Rule 144A(d)(4) of the U.S. Securities Act of 1933 also requires certain information about the issuer (for example, financial statements, business description) to be made available upon request to prospective purchasers as a condition of eligibility for Rule 144A's exemption from registration, but the prevailing market view has been that a passworded website would meet this requirement so long as passwords to the information were available to prospective purchasers as well as existing investors.

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