SEC Approves Relaxed Pricing Limits for NYSE and NASDAQ Primary Direct Floor Listings

Alert
01.04.2023

On December 15, 2022, the Securities and Exchange Commission (SEC) relaxed price range limitations when it approved a proposed rule change set forth by the New York Stock Exchange (NYSE) for companies listing in connection with primary direct floor listings. Following a similar rule change for the Nasdaq on December 2, 2022, the modified rule for each exchange allows the opening auction to proceed at a price up to either 20% below or 80% above the disclosed price range subject to certain conditions.

PRIMARY DIRECT FLOOR LISTINGS AND THE MODIFIED RULES

The NYSE and Nasdaq adopted rules allowing for primary direct floor listings in 2020 and 2021; however, there has not been a primary direct floor listing to date on either exchange. A company that has not previously had its common equity securities registered under the Exchange Act may wish to list its common equity securities on the exchange at the time of effectiveness of a registration statement pursuant to which the company will sell shares itself in the opening auction on the first day of trading on the exchange. One potential benefit of a primary direct floor listing as an alternative to a traditional initial public offering (IPO) is that it could maximize the chances of more efficient price discovery of the initial public sale of securities for issuers and investors.

In contrast to a traditional IPO, where the offering price is apprised by underwriter engagement with potential investors to determine the interest in an offering, but ultimately decided through negotiations between the issuer and the underwriters for the offering, the initial sale price in a primary direct floor listing is determined based on market interest and the matching of buy and sell orders in an auction open to all market participants.

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While many companies are interested in alternatives to the traditional IPO, companies and their advisors may be reluctant to use the primary direct floor listings under existing NYSE and Nasdaq rules due to issues with price range limitations, among other hurdles.

Under the existing rule, during the auction process for a primary direct floor listing, a company must disclose a price range and the number of shares to be sold in the registration statement, and the opening auction price must be within the disclosed price range. In effect, a company participating in a primary direct floor listing is prevented from opening trading at a price below the bottom end of the price range or above the top end of the price range without filing an amendment to the registration statement.

Therefore, if an offering is unable to be completed due to lack of investor interest, the offering may be delayed or cancelled. The price range limitation that was imposed on a primary direct floor listing but not on an IPO increased the probability of a failed offering because it "contemplated there also being too much investor interest."

Now, the modified rules allow the opening auction to proceed at a price up to either 20% below or 80% above the disclosed price range subject to certain conditions. This enhances the prospects for primary direct floor listings by creating flexibility around the issuer's stock price at the time of listing.

DISCLOSURE AND CERTIFICATION REQUIREMENTS

Under both the NYSE and Nasdaq, for a company to be able to proceed with a primary direct floor listing when the auction price falls outside of the stated price range but within the modified price range, the company must satisfy certain requirements, including:

- The company must have certified to the respective exchange and publicly disclosed that the company does not expect that the auction price would materially change the company's previous disclosure in its effective registration statement.
- The effective registration statement covering the shares must include a sensitivity analysis explaining how the issuer's plans would change if the actual proceeds from the offering differ from the amounts assumed within the stated price range.
- The company must confirm to the applicable exchange that no additional disclosures are required under federal securities laws based on the auction price in circumstances where the actual price calculated is outside of the disclosed price range.

Additionally, the NYSE requires certification that the price range in the preliminary prospectus included in the effective registration statement is a bona fide price range in accordance with Item 501(b)(3) of Regulation S-K.

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ISSUER MUST RETAIN AN UNDERWRITER

Both the NYSE's and Nasdaq's modified rules require a company offering securities for sale in connection with a primary direct floor listing to retain an underwriter with respect to the primary sales of shares, and to identify the underwriter in its effective registration statement.

Although the delegated underwriter will not perform traditional underwriting services, each exchange stated that the underwriter "would perform substantially similar functions, including those related to establishing and adjusting the price range, to those performed by an underwriter in a traditional IPO because the underwriter will be subject to similar liability and reputational risk."

Also, the SEC thinks that the existence of an underwriter will help mitigate traceability concerns for Section 11 liability purposes because the underwriter will be able to impose lock-up arrangements similar to those in traditional IPOs.

PRICE DISCOVERY TRANSPARENCY

Because the modified rules for both the NYSE and Nasdaq allow the auction price to fall outside the stated price range, both exchanges recognized the need for better transparency around price discovery during the auction. Thus, on the day of the auction both exchanges will provide investors access to real-time pricing information on a public website, and in the case of the NYSE rules, the pricing information will also be provided on a proprietary data feed prior to the auction date.

PRICE VOLATILITY CONSTRAINT

The most notable difference between the proposals by the NYSE and Nasdaq relates to price volatility. While the NYSE did not adopt new rules to address price volatility, the Nasdaq adopted a "Price Volatility Constraint" which would require that the current reference price (the price at which the maximum number of shares are paired based on investors' indications of interest) not have deviated by 10% or more from any current reference price during the pre-launch period within the previous 10-minute period (such price once the Price Volatility Constraint is satisfied, the "Near Execution Price"). The pre-launch period would continue until at least five minutes after the Price Volatility Constraint has been satisfied, during which time, investors will be able to modify their orders prior to the finalization of the opening auction and the pricing of the offering.

Additionally, the pricing may not execute if the final execution price as determined by the orders placed during such period exceeds 10% above or below the Near Execution Price, a range designate the "Price Collar." If, as a result of the final execution price falling outside the 10% Price Collar, the security is not released within 30 minutes of the Near Execution Price being initially satisfied, the Price Volatility

Constraint will reset, and all requirements of the pre-launch period will need to be met again.

CONCLUSION

Although it is unclear whether the modified rules will cause companies to begin utilizing primary direct floor listings in going public, the modified rules are an important step towards that direction.

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