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### Better practices for licensees

- D1 We encourage licensees to:
- (a) discuss and set out in writing the approach to allocations with the issuer at various stages during the transaction. This may include providing the issuer with a copy of the licensee's allocation policy;
  - (b) identify conflicts in relation to allocations, disclose them to the issuer and explain how they are to be managed;
  - (c) have a reasonable basis for allocation recommendations and ensure they are consistent with the issuer's objectives;
  - (d) provide issuers with information about the bids submitted, the investors who have submitted these bids and the rationale for the allocation recommendation. This information should be accurate and not misleading or deceptive; and
  - (e) disclose to the issuer details of any proposed allocations to employees or principal accounts of the licensee and its related entities and the rationale for these allocations. These allocations should be separately disclosed and not aggregated with other investors.

Note: Also see the better practices for allocations to employees and principal accounts set out in F2.

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### Better practices for issuers

- D2 Issuers are encouraged to understand and engage with the allocation process. This could include:
- (a) discussing the approach to allocations with the licensee at various stages during a transaction (e.g. pitching, marketing and when the allocation recommendation is provided by the licensee);
  - (b) for secondary capital raisings, considering the treatment of existing security holders (including passive investment funds) in allocation decisions;
  - (c) for rights issues, considering the potential control implications of the offer structure, shortfall mitigation strategy and underwriting arrangements;
  - (d) considering the inclusion of a provision in the terms of engagement about how allocation decisions are made and approved, including a clear statement of the role of the issuer in the allocation process;
  - (e) asking the licensee to provide a copy of their allocation policy;
  - (f) asking the licensee to explain how the allocation recommendation is consistent with their allocation policy and the issuer's objectives;
  - (g) asking the licensee questions about the allocation recommendations, including:
    - (i) the rationale for the allocation recommendation;

- (ii) details of proposed allocations to employees and principal accounts and the rationale for these allocations; and
  - (iii) details of proposed allocations to related investment managers; and
- (h) scrutinising and querying the basis for any advice or statements in draft ASX announcements about the transaction, in particular about the nature and level of demand from investors. The use of overly expressive language should be avoided.

## E Messages to investors

### Key points

This section outlines our findings on messages provided by licensees to investors in connection with transactions. This includes:

- messages provided when marketing begins;
- any update messages provided during the bookbuild; and
- feedback provided to investors following the allocation process.

We also outline feedback on the content of any ASX announcements released by issuers about the nature and level of demand from investors for a transaction.

The section sets out better practices in relation to messages by licensees and issuers in connection with transactions.

- 162 Licensees and issuers often provide messages to investors about transactions, which can help them make investment decisions.
- 163 Messages are often provided about the level of demand and likely price at which securities will be issued during the marketing of a transaction and after allocations are determined.
- 164 Poor conduct around messages provided to investors during marketing about the status of an offer, or after the offer closes about the level of demand and extent of any scale-backs, may breach prohibitions in Pt 7.10 of the Corporations Act and Pt 2 of the ASIC Act relating to misleading and deceptive conduct.
- 165 Issuers also need to be mindful of these requirements when making statements in market announcements about the level of demand for a transaction and consider their continuous disclosure obligations: see s674 of the Corporations Act and the requirements of the relevant exchange (e.g. ASX Listing Rule 3.1).

### Messages from licensees

- 166 Licensees contact eligible investors to seek bids for transactions. This is usually undertaken by the licensee's sales desk which has received a briefing by the licensee's ECM team. There are some differences in approach across the licensees we sampled.

## At commencement of marketing

167 At the commencement of marketing, the sales desk typically sends eligible investors an electronic message setting out key information about the offer (initial message). This information is usually prepared by the ECM team, goes through an internal review process (which may include review by legal counsel and the issuer) and is sent to eligible investors at around the same time.

## Update messages

168 During the marketing of an offer, the licensee may decide to provide a formal update message about the level of demand and the likely price at which securities will be issued (update message).

169 The update message may include a comment by the licensee that the offer is ‘covered’, ‘well covered’, ‘cornered’, or similar wording. These terms are intended to give confidence to investors that an offer has been well received.

170 We found that licensees and institutional investors interpret ‘covered’ to mean that total bids have been received from investors that are capable of being allocated (allocable demand) for at least the total amount being sought under the offer.

171 Some licensees advised that they also use the term ‘well covered’ in updates. Most licensees understood ‘well covered’ to mean that the transaction has received bids for twice or more than twice the amount being sought. Other licensees noted that 1.2 to 1.5 times the amount being sought could be ‘well covered’ if the bids were from high-quality institutional investors.

172 Most institutional investors advised us that they want to know if a transaction is ‘covered’ as it indicates the level of investor support for a transaction and, more importantly, means that the licensee will not be left holding shortfall securities in the after-market. Other institutions commented that they do not rely on messages from licensees and make their own assessments of the merits of an offer.

173 In determining the level of allocable demand, we found that the ECM team accepts bids submitted by its sales desk at face value, relying on the sales desk to ensure these bids are capable of acceptance in full, and excludes bids from related investment managers, employees and principal accounts.

174 We observed the following practices regarding update messages:

- (a) update messages are not always provided, and this can depend on the offer type, size and level of demand;



- (b) some licensees adopt a formal process for update messages (including approval by a senior employee in the ECM team), whereas other licensees have no formal guidelines or process for update messages;
- (c) update messages are generally provided to investors who have expressed interest or are likely to express interest in the offer;
- (d) update messages are generally provided verbally and are not delivered to investors at the same time;
- (e) update messages typically include information about the level of demand for the offer and the likely clearing price. Examples of update messages include: ‘the offer is covered at the top end of the range’ and ‘the offer has received strong support and participation from existing security holders—strong bidding has also been seen from non-holders’;
- (f) several large licensees have policies that set out guidelines for update messages, including:
  - (i) update messages must be fair and not misleading, limited to factual matters and avoid inflammatory language. For example, ‘overwhelming demand’ was not permitted but ‘well covered’, ‘fully covered’ or ‘multiple times covered’ were permitted;
  - (ii) update messages may provide a general description of the investors who are bidding (e.g. ‘strong domestic interest’ or ‘strong support from global long only and hedge funds’) but not provide specific splits;
  - (iii) if a book is partially covered, some licensees allow statements such as ‘the book is one-third covered’, ‘the book is 80% covered in the middle of the range’ or ‘bids lower than a certain price will not receive an allocation’; and
  - (iv) consideration needs to be given to obligations of client confidentiality in providing updates;
- (g) licensees noted a level of caution about providing update messages given the dynamic nature of a bookbuild and ASIC’s focus on this area; and
- (h) licensees have a range of practices when confronted with the situation where a previous message is no longer correct. Most licensees could not clearly articulate how they manage this situation. The policy of one licensee required the ECM team to consider whether a further communication was needed and, depending on the nature of the change, escalate the matter to compliance.

## Feedback following allocations

- 175 Following completion of the allocation process, licensees contact investors who have bid for securities to confirm the allocation to be provided to the investor (post-allocation message). At this time, we noted it is common for the licensee to provide feedback to the investor about the nature and level of demand for the offer. For example, the ‘offer was strongly supported by a range of new and existing security holders’ or ‘the issuer wanted to bring some new institutional investors onto the register’.

## Messages from issuers

- 176 On completion of an IPO and before listing, issuers are required to make pre-quotation disclosures to the relevant exchange. For listings on the ASX this includes a list of the top 20 security holders and a distribution schedule showing the spread of investors by size of holding.
- Note: Investors are also subject to reporting obligations in relation to substantial security holdings set out in Ch 6C of the Corporations Act.
- 177 For secondary capital raisings, issuers must disclose information (under their continuous disclosure requirements) about transactions to the relevant exchange. There is often commentary about the level and nature of investor demand (e.g. ‘the offer was heavily subscribed with strong support from both existing security holders and new investors’). For IPOs, we observed that it was less common for the issuer to release a market announcement which included a comment about the level and nature of demand for the offer.
- 178 Some institutional investors expressed concern with statements in market announcements about the level and nature of investor demand. They cited examples where offers that were communicated as being ‘heavily oversubscribed’ traded at a discount to the issue price in the after-market. This might suggest that the demand from investors was not as strong as stated in the announcement.
- 179 We were advised that issuers rely on information provided by licensees to support statements about the nature and level of investor demand contained in market announcements.
- 180 Institutional investors also provided feedback that they see the allocation process as a ‘black box’. They understood that for keenly sought after offers it was not possible for all investors to receive their desired allocation, but they suggested they would have greater confidence in the process if there was more transparency about allocation outcomes.

- 181 Institutional investors suggested that transparency of allocations would be improved if market announcements by issuers included:
- (a) the total number of securities allocated to employees and principal accounts of licensees (and their related entities) involved in the transaction (where transactions are oversubscribed); and
  - (b) for secondary capital raisings:
    - (i) details of the split of allocations between new and existing security holders; and
    - (ii) a list of the top 20 allocations, with the names of investors removed.

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### Better practices for licensees

- E1** We expect licensees to:
- (a) have clear processes and responsibilities as to who can provide messages in relation to transactions. This includes the preparation and review of messages to ensure they do not contain misleading or deceptive information;
  - (b) send messages to investors at the same time or as close together as practical;
  - (c) provide any messages in writing;
  - (d) ensure communications by employees of the licensee to investors are consistent with the messages provided by the ECM team;
  - (e) have a reasonable basis for any messages that a transaction is 'covered' or 'cornered' (or other similar wording). In determining this, bids from related investment managers, employees and principal accounts, and any bids that the licensee deems excessive (considering their knowledge of the investor), should be excluded;
  - (f) provide an update message if previously communicated information is or becomes inaccurate; and
  - (g) ensure they are accurate and not misleading or deceptive in any feedback provided in the post-allocation message.

For the purpose of this section, messages include update messages.

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### Better practices for issuers

- E2** When preparing market announcements that comment on the nature and level of demand for a transaction, we expect issuers to:
- (a) ensure these statements are accurate and not misleading—the use of overly expressive language should be avoided; and
  - (b) make appropriate inquiries of the licensee to understand the composition of the demand and understand if it includes any inflated or exaggerated bids or bids from related investment managers, employees or principal accounts.

## F Allocations to parties connected to the licensee

### Key points

This section outlines our findings on the approach licensees adopt in allocations to parties connected to them, including related investment managers, employees and principal accounts.

This is a high-risk area for conflicts of interest and we set out better practices for licensees.

We also set out our findings on how licensees handle transactions introduced by employees outside of the ECM team.

- 182 Allocations to related investment managers and employees and principal accounts raise significant conflicts of interest concerns.
- 183 Licensees are gatekeepers who are paid by issuers to manage transactions. In this role, they obtain information about the overall level of demand for transactions and the interest expressed by investors. They also obtain an indication of the likely after-market demand for an issuer's securities. This places licensees at a significant information advantage compared to investors who bid for securities in transactions.
- 184 Allocations to employees and principal accounts also have the potential to influence decisions of the licensee (e.g. advice to clients and research decisions). This may result in advice being provided that may not be in the best interests of the issuer or the licensee's investing clients.

### Allocations to related investment managers

- 185 Some licensees have related entities that manage funds on behalf of third-party investors (for this report we refer to these as 'related investment managers').
- 186 We observed that most large licensees had a process—often reflected in policies and procedures—for managing bids and allocations by related investment managers. This included:
- (a) providing related investment managers and other investors with the same information at the same time;
  - (b) ensuring that bids by related investment managers follow the same process as other institutional investors (e.g. when bids are due);
  - (c) not giving preferential treatment to related investment managers; and

- (d) making sure that allocations to related investment managers are consistent with the issuer's objectives and disclosed to the issuer.

187 In transactions we reviewed, related investment managers typically did not receive an allocation. Where an allocation was made to a related investment manager, we observed that the scale-back applied to these bids was similar to that applied to comparable unrelated investors.

### Better practices

- F1** Licensees should have policies and procedures to manage the treatment of bids by related investment managers when making allocation recommendations, including:
- (a) clearly identifying related investment managers;
  - (b) treating related investment managers in the same manner as other investors, for example:
    - (i) ensuring information about the transaction (including the level of demand) is the same as that provided to other investors;
    - (ii) providing information about the offer to both related investment managers and other investors at the same time;
    - (iii) following the same process for bids by related investment managers as for other investors; and
    - (iv) applying scale-backs and allocation recommendations for related investment managers on a similar basis to comparable unrelated investors; and
  - (c) ensuring allocations to related investment managers are disclosed to the issuer and are consistent with the issuer's objectives.

## Allocations to employees and principal accounts

188 We observed that licensees who are managing transactions sometimes allocate securities to:

- (a) themselves or related entities (for the purposes of this report we refer to these as 'principal accounts'); or
- (b) directors, employees or contractors of the licensee or their related bodies corporate or immediate family (for the purposes of this report we refer to these as 'employees').

Note 1: Principal accounts include any allocation to a licensee's trading desk to help with market-making or facilitation activities.

Note 2: Market participants should also see the definition of 'principal' in the ASIC Market Integrity Rules (Securities Markets) 2017 (Securities Markets Rules) for further information.

189 Where securities are allocated to employees and principal accounts in an oversubscribed offer, the allocation that would otherwise be provided to other investors, including clients of the licensee, is reduced.

### Large licensees

190 In general, large licensees do not allow allocations to employees in transactions they are involved in as they can lead to significant conflicts of interest.

191 Large licensees also advised that allocations to principal accounts are not common and tend to be limited to shortfalls in transactions the licensee is underwriting.

192 We observed that most large licensees have policies and procedures for bids by principal accounts, including:

- (a) providing principal accounts and other investors with the same information at the same time;
- (b) submitting bids from principal accounts before the offer opens (or very early in the process) unless the offer is undersubscribed or the allocation results from an underwriting obligation. Any exceptions to this requirement are subject to internal committee and compliance approval;
- (c) in the case of some licensees, prohibiting amendments to the price and size of principal account bids once submitted. Other licensees allow amendments subject to approval by compliance and the head of the desk;
- (d) placing limits on the size of allocations to principal accounts;
- (e) disclosing bids from principal accounts to the issuer in the transaction documentation and in any allocation recommendation provided to the issuer for approval;
- (f) ensuring that bids from principal accounts do not materially affect the pricing of the offer;
- (g) considering their conflicts of interest obligations in relation to allocations to principal accounts. For example, where a transaction can be allocated to external investors, the licensee should consider the appropriateness of a principal allocation;
- (h) scaling back bids by principal accounts to the same (or a greater) extent as for other unrelated investors; and
- (i) limiting any buffer in size and allocating it to unrelated investors before the securities commence or recommence trading.

Note: Also see [Report 452](#) *Review of high-frequency trading and dark liquidity* (REP 452) for ASIC guidance on managing order flow and conflicts of interest when engaging in principal trading and facilitation activities.

## Mid-sized licensees

193 At mid-sized licensees, allocations to employees occurred in most transactions we reviewed but allocations to principal accounts were less common.

194 Most institutional investors did not believe employees should receive allocations given the information that licensees receive about the nature and level of demand for a transaction. Other institutional investors did not believe that allocations to staff accounts presented a conflict, provided they were adequately disclosed, limited in size and subject to appropriate internal controls.

195 Our review found:

- (a) licensees advised that allocations to employees:
  - (i) help an issuer undertaking an IPO to meet the spread requirements of the relevant exchange;
 

Note: Issuers and licensees should be aware that the spread requirement in ASX Listing Rule 1.1, condition 8 'is not met if spread is obtained by artificial means': see ASX Guidance Note 1 *Applying for Admission – ASX Listings* at Section 3.8 'Minimum spread'.
  - (ii) make up the balance if an offer is undersubscribed; and
  - (iii) give retail investors and HNW investors comfort knowing that their adviser has 'skin in the game';
- (b) there was limited disclosure to the issuer about allocations to employees. Some licensees include general wording in terms of engagement that employees may receive an allocation. We found it was more common for allocations to employees to be aggregated with retail investors and HNW investors;
- (c) in some instances, licensees had not correctly designated accounts as employee accounts;
- (d) the ECM team preparing the allocation recommendation sometimes included an allocation of securities for themselves;
- (e) not all mid-sized licensees had policies and procedures for allocations to employees. Those that did provided that:
  - (i) bids from employees would be excluded when there was excess demand from client bids. In our transaction review we did not see this occur despite some offers being multiple times oversubscribed;
  - (ii) dollar caps would be imposed on allocations to employees where an offer was oversubscribed;
  - (iii) employee bids would be scaled back by at least the same amount as client bids. Nonetheless, we observed a placement where

employees were scaled back by less than bids from HNW investor clients of a licensee;

- (iv) a small buffer may be retained to manage errors or omissions. We observed that this was allocated to investors, or in a few instances to the licensee's ECM team or to the adviser who introduced the transaction to the licensee;
- (v) bids by employees had an internal approval process (e.g. compliance or the CEO);
- (vi) bids from employees were submitted to the ECM team before the commencement of the bookbuild for the transaction; and
- (vii) there were a range of practices for holding periods for allocations to employees, including no holding period through to 28 days.

### Better practices for licensees

- F2** Allocation recommendations to employees and principal accounts present a significant risk of conflict with the interests of both the issuer and the licensee's investing clients.

It is better practice to avoid this conflict except where an offer is undersubscribed and the allocation is limited to the extent necessary for the issuer to raise the funds sought.

Note: Also see the better practices outlined in F1 and E1 in relation to messages to investors.

Licensees that propose an allocation to employees and principal accounts need robust policies and procedures to manage conflicts, including consideration of:

- (a) its appropriateness, bearing in mind the level and quality of demand received from investors for the offer;

Note: For example, imposing caps on the number of securities that can be allocated to employees and principal accounts or excluding these allocations entirely.

- (b) disclosure to the issuer of any allocation proposed to employees and principal accounts;

Note: For example, separately listing the total number of securities to be allocated to employees and principal accounts in the allocation recommendation provided to the issuer for approval.

- (c) other than where an offer is undersubscribed, disclosure by licensees to investors who received an allocation of any allocation made to employees and principal accounts;

Note: For example, when advising clients of their allocation, provide details of the total number of securities allocated to employees and principal accounts.

- (d) the timing and process for submitting bids by employees and principal accounts to the ECM team. It is better practice to submit



these bids early in the process and, at a minimum, before the commencement of the bookbuild for the transaction;

- (e) appropriate minimum holding periods for any securities allocated to employees and principal accounts (e.g. at least several weeks);
- (f) internal approval processes for bids by and allocation recommendations to employees and principal accounts;
- (g) monitoring and review arrangements, including enforcement of minimum holding periods; and
- (h) treatment of any buffer—it is better practice to allocate these securities to unrelated investors before the issuer's securities recommence trading.

Licensees should ensure that employees and principal accounts are correctly designated as such.

## Transactions introduced by public-side employees

- 196 We observed at times that employees from the public (or trading) side of a licensee may introduce a potential transaction to the licensee. Where this occurs, the more common approach is for the employee to refer the opportunity to the licensee's ECM team who market the transaction through their usual distribution channels (ECM managed).
- 197 A less common approach is where the employee from the public side of the licensee leads the transaction. This may include advising the issuer on pricing and terms and managing allocations with limited input from the licensee's ECM team (advisor managed).
- 198 We observed an advisor-managed transaction where:
- (a) an employee from the public side of the licensee managed the transaction and allocated a large number of securities to himself and to his related entities;
  - (b) the licensee did not correctly designate the employee's trading accounts as employee accounts;
  - (c) the transaction was not marketed through the licensee's usual distribution channels, but was limited to a smaller number of investors skewed to clients of the employee managing the transaction; and
  - (d) the employee collected around 90% of the fees generated by the licensee for the transaction.
- 199 We have concerns with the advisor-managed model given the inherent risk of mishandling inside information and mismanaging conflicts.

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### Better practices for licensees

- F3** Where an employee on the public side of the licensee identifies or becomes aware of a potential transaction, it is better practice for these opportunities to be passed to the licensee's ECM team to manage.

Note: The ECM team may decide at a later stage to wall-cross the employee who introduced the transaction to help with distribution of the offer.

Licensees should have effective arrangements (managed by compliance or another control function) for wall-crossing staff who come into possession of inside information.

We encourage firms to review their remuneration structures to ensure they do not incentivise public-side employees to seek out or discuss corporate advisory matters involving inside information with listed companies.

## Appendix 1: International regulatory approaches

### Background

200 Australia operates under a principles-based approach to financial services regulation: see [ASIC's Statement of Intent 2018](#). Examples of this include the obligation for AFS licensees to manage conflicts and provide financial services efficiently, honestly and fairly: s912A of the Corporations Act.

201 The principles-based approach is supplemented, where appropriate, by regulatory guidance. This guidance explains how we interpret the law, describes the principles underlying our approach, and provides practical guidance to the regulated population.

### International Organization of Securities Commissions

202 In September 2018, IOSCO published guidance addressing the potential conflicts of interest and associated conduct risks in the equity capital raising process: see IOSCO's report, [Conflicts of interest and associated conduct risks during the equity capital raising process](#) (PDF 353 KB).

203 The guidance details the key stages of transactions where the role of financial intermediaries might give rise to conflicts of interest that compromise the integrity and efficiency of the process. The guidance comprises eight measures that address:

- (a) conflicts of interest and pressure on analysts during the formation of their views on an issuer in the pre-offering phase of a capital raising;
- (b) conflicts of interest during the allocation of securities;
- (c) conflicts of interest and conduct risks in the pricing of securities offerings; and
- (d) conflicts of interest and conduct risks stemming from personal transactions by staff employed within firms managing a securities offering.

204 The guidance is the first stage of IOSCO's work in examining conflicts of interest and associated conduct risks in the capital raising process. The second phase will consider conflicts of interest and associated conduct risks during the debt capital raising process.

### United States

205 The Financial Industry Regulatory Authority (FINRA) rules are designed to promote transparency and establish conduct standards in the capital raising process.

Note: Every firm and broker that sells securities to the public in the United States must be licensed and registered by FINRA.

- 206 [FINRA Rule 5130](#) (Restrictions on the purchase and sale of initial public equity offerings) prohibits restricted persons (e.g. broker-dealers and their immediate family members) from participating in new issues of securities (subject to a limited number of exceptions).
- 207 [FINRA Rule 5131](#) (New issue allocations and distributions) is intended to support public confidence in the IPO process by establishing requirements with respect to the allocation, pricing and trading of new issues by member firms. The rule is subject to specified exceptions.
- 208 Rule 5131 prohibits:
- (a) *quid pro quo allocations*—using the IPO allocation process to receive excessive compensation for services provided;
  - (b) *spinning*—allocating IPO shares to any account in which an executive officer, director and certain former or prospective investment banking client or a person materially supported by such executive officer or director, has a beneficial interest. Firms are required to establish, maintain and enforce policies and procedures that are reasonably designed to prevent investment banking personnel from indirectly or directly influencing or being involved in their firm’s new issue allocation decisions;
  - (c) *levying penalties on flipping*—firms trying to recoup a portion of the commission paid from investment advisers whose clients sell IPO shares they were allocated soon after listing (unless the managing underwriter has assessed a penalty bid on the entire syndicate); and
  - (d) *acceptance of market orders*—members soliciting or accepting market orders for the purchase of IPO shares in the secondary market before the start of trading.
- 209 Distribution participants also need to comply with Rule 101 of the Securities and Exchange Commission (SEC)’s Regulation M under the *Securities Exchange Act 1934*. This rule focuses on securities distributions and, with some exceptions, prohibits distribution participants from engaging in certain trading activities that could artificially raise the price of a security or create a false appearance of active trading in the market, including:
- (a) soliciting from clients their intention to place an after-market order and the quantity of the order before the completion of the securities distribution;
  - (b) telling clients that purchasing shares in the after-market would help them obtain an allocation in other popular IPOs;
  - (c) encouraging investors that have indicated an interest in after-market purchases to increase the price they would be willing to pay because other customers have provided higher after-market price limits; and

- (d) rewarding clients for placing after-market orders by allocating additional IPO shares to them.

210 As part the FINRA360 review, FINRA released a [progress report](#) advising that it was preparing to file amendments to FINRA Rule 5130 and Rule 5131 with the SEC. The amendments would remove a range of impediments to capital formation that it considered to be unnecessary to protect investors. The proposed amendments would also exempt additional persons and types of transactions from the scope of the rules, modify current exemptions to enhance regulatory consistency and address unintended operational issues: see [Progress report on FINRA360](#) (PDF 398 KB), April 2018.

### United Kingdom

211 The Financial Conduct Authority (FCA) has published the [Conduct of Business Sourcebook](#). Chapter 11A.1 sets out rules and guidance for underwriting and placing applicable to Markets in Financial Instruments Directive (MiFID) or equivalent third country business (in the European Union), including references to Articles 38–43 of the MiFID II Delegated Regulations: see section on ESMA (paragraphs 215–217).

212 In October 2016, the FCA published the findings of a review of the factors that influence IPO allocations to investors: see FCA, [Quid pro quo? What factors influence IPO allocations to investors?](#) (PDF 2.72 MB), Occasional paper 15. The review sought to understand if the IPO allocation process works in the interest of issuers or whether conflicts of interest may result in investment banks favouring their highest-revenue clients when deciding on final allocations in IPOs.

213 Key findings were:

- (a) syndicate banks make favourable allocations to investors who provide them with information likely to be useful in pricing the IPO, particularly investors who submit price-sensitive bids and those who attend meetings with the issuer before the IPO;
- (b) book-runners made favourable allocations to investors from whom they generate the greatest revenues elsewhere in their business, notably through brokerage commissions;
- (c) long-only investors seem to receive more favourable allocations than hedge funds; and
- (d) there was no evidence that banks make less favourable allocations to investors who go on to sell those shares shortly after the IPO, or that they favour investors who provide after-market liquidity.

214 The FCA also found there is no unique optimal allocation or pricing policy for each IPO, and so it is difficult to quantify the extent, if any, to which

allocating shares to banks' preferred clients leads to a less favourable outcome for issuers.

### European Securities and Markets Authority (ESMA)

- 215 [MiFID II](#) came into effect on 3 January 2018. Provisions relevant to allocations are generally addressed through the conflicts of interest regulations—in particular, Articles 38 to 43 of the MiFID II Delegated Regulation.
- 216 Key requirements for firms that provide underwriting or placing of financial instruments include:
- (a) providing specified information to issuers before accepting a mandate to manage an offering, including the timing and process for the offer and details of targeted investors;
  - (b) identifying all underwriting and placing operations provided by the firm, and ensuring that adequate controls are in place to manage any potential conflicts of interest;
  - (c) implementing and maintaining effective arrangements to prevent recommendations on placing from being inappropriately influenced by any existing or future relationships (e.g. laddering and spinning);
  - (d) establishing, implementing and maintaining effective internal arrangements to prevent or manage conflicts of interests that arise where persons responsible for providing services to the firm's investment clients are directly involved in decisions about recommendations to the issuer client on allocations; and
  - (e) setting out record-keeping requirements in relation to an underwriting or placing.
- 217 On 3 October 2018, ESMA released [Questions and answers on MiFID II and MiFIR investor protection topics](#). The purpose of this document is to promote common supervisory approaches and practices in the application of MiFID II and MiFIR in relation to investor protection topics. It provides responses to questions posed by the general public, market participants and competent authorities in relation to the practical application of MiFID II and MiFIR. Section 6 includes information about underwriting and placing.

### Hong Kong

- 218 The Hong Kong Stock Exchange (HKSE) Main Board Listing Rules permit a new issue of shares to be offered by way of 'placing' unless there is likely to be significant public demand for the securities.
- 219 [Practice Note 18](#) (Initial public offer of securities) sets out certain procedures to be adopted in the allocation of shares in IPOs. It also sets out certain

procedures to be adopted where an IPO involves a placing tranche and public subscription tranche of securities.

- (a) The total number of securities available for public subscription (taking account of any clawback feature in the case of issues which involve both placement and public subscription tranches) are to be divided equally into pools: pool A and pool B:
  - (i) Pool A—securities in pool A should be allocated on an equitable basis to applicants who have applied for securities in the value of HK\$5 million or less.
  - (ii) Pool B—securities in pool B should be allocated on an equitable basis to applicants who have applied for securities in the value of more than HK\$5 million and up to the value of pool B.
- (b) Where one of the pools is undersubscribed, the surplus securities should be transferred to satisfy excess demand in the other pool and be allocated accordingly.

220 No applications should be accepted from investors applying for more than the total number of shares originally allocated to each pool. Multiple applications within either pool or between pools should be rejected.

221 Placements are covered by Appendix 6 ‘Placing guidelines for equity securities’ of the Main Board Listing Rules. The key points are:

- (a) the securities to be placed must have an adequate spread of holders, the number depending on the size of the placing, but as a guideline there should be not less than three holders for each HK\$1,000,000 worth of the share issue, with a minimum of 100 holders at the time of listing (paragraph 4 of Appendix 6);
- (b) neither the lead broker nor any distributor may retain any material amount of the securities being placed for their own account; and
- (c) where there is public demand, neither the lead broker nor any distributor may retain more than 5% of their respective shares of the total placing. Where securities are made available by the lead broker direct to the general public by application direct to the lead broker and there is insufficient public demand, the amount not taken up can be redistributed to clients of the lead broker.

## Singapore

222 The Singapore Exchange Limited (SGX) maintains a range of rules for allocations in transactions. [Part IX of Chapter 2](#) of the Mainboard Rules includes the following requirements:

- (a) *public subscription tranche*—all IPOs must include a public subscription tranche (being a minimum of 5% or S\$50 million

















## Related information

### Headnotes

advisers, allocations, bookbuild, capital raisings, conflicts of interest, dividend reinvestment plans, employees, entitlement offer, information barriers, initial public offerings, inside information, insider trading, IPOs, joint lead manager, listed entities, non-renounceable, placements, principal trading, pro rata, renounceable, secondary capital raisings, security purchase plans, soundings, wall-crossing

### Regulatory guides

[RG 6](#) *Takeovers: Exceptions to the general prohibition*

[RG 104](#) *Licensing: Meeting the general obligations*

[RG 181](#) *Licensing: Managing conflicts of interest*

[RG 240](#) *Hedge funds: Improving disclosure*

[RG 264](#) *Sell-side research*

### Legislation

ASIC Act, Pt 2; s12DA and 12DB

Corporations Act, Pt 7.10; s124, 180, 181, 184, 674, 710, 734, 912A, 1041A, 1041H, 1042A, 1043A and 1043B–1043K

### Reports

[REP 393](#) *Handling of confidential information: Briefings and unannounced corporate transactions*

[REP 486](#) *Sell-side research and corporate advisory: Confidential information and conflicts*

[REP 512](#) *ASIC regulation of corporate finance: July to December 2016*

[REP 540](#) *Investors in initial public offerings*

### Consultation papers

[CP 46](#) *Licensing: Managing conflicts of interest*

[CP 128](#) *Handling confidential information*

[CP 290](#) *Sell-side research*