UKLA Technical Note

Compliance with the Listing Principles and Premium Listing Principles

Ref: UKLA / TN / 203.2

LR 2.2.4R and LR 7

The Listing Principles and Premium Listing Principles, which are set out in LR 7, are a general statement of the fundamental obligations of listed companies. Companies with a standard listing ~~of their equity shares~~ must comply with the Listing Principles. Companies with a premium listing of their equity shares must, in addition, comply with the Premium Listing Principles. They were introduced to ensure adherence to the spirit as well as the letter of the various rules, including the Disclosure and Transparency Rules, comprising the listing regime.

Issuers should therefore be aware of the importance we place on complying with the Principles on an ongoing basis. As our Handbook notes, breaching a Listing Principle or Premium Listing Principle will make a listed company liable to disciplinary action by us. While cases may be brought in conjunction with action for a breach of a specific rule or rules, we are prepared to take enforcement action on the basis of the Principles alone, taking account of the standard of conduct required by the Principle in question.

LR 7.2.1AR: Articles containing compulsory acquisition provisions

Compulsory acquisition or redemption powers need to be considered carefully to ensure they do not offend the principle of equality of treatment of all shareholders in LR 7.2.1AR (Premium Listing Principle 5) if they do not generally treat shareholders equally. Please see LR 2.2.4R for further details about such powers.

UKLA Technical Note

Hostile takeovers

Ref: UKLA / TN / 305.2

LR 10.5.2R, LR 13.4.1R, LR 13.4.3R, LR 13 Annex 1 and PR Appendix 3 Annexes

Non-recommended offers / limited access

The following sets out our approach to non-recommended offers and covers their treatment in certain areas of the Listing and Prospectus Rules. Such offers are characterised by restrictions on access to information on the offeree business, assets or undertaking to be acquired.

The general principle underpinning our approach is that where a listed offeror cannot gain access to the relevant offeree information, the offeror should seek out and publish the best information available to it. In these circumstances, the offeree information contained in prospectuses or circulars can be based on published sources.

Class 1 circulars

The following items cover some of the typical issues we have encountered in hostile and limited access situations under the Listing Rules:

Responsibility statement

LR 13.4.3R(4) allows information on the offeree to be disclosed on the basis of information published (or made available) by the offeree and that the issuer is aware of and free to disclose.

Accordingly, we have accepted examples of modifications to responsibility statements such as:

'(Offeror's directors and proposed directors) accept responsibility for the information contained in this document, except that the only responsibility accepted by (offeror's directors and proposed directors) in relation to (offeree), which has been compiled from published sources (or made available), is to ensure that such information is correctly and fairly produced and presented. To the best of the knowledge and belief of the (offeror's directors and proposed directors) (who have taken all reasonable care to ensure that such is the case) the information contained in this document (other than the information contained in this document relating to (offeree)) is in accordance with the facts and does not omit anything likely to affect the import of such information.'[1]

LR 13 Annex 1 statements

LR 13 Annex 1 statements for material contracts, litigation and significant change required on the offeree are also usually modified using the phrase:

'As far as (offeror) is aware, having regard to published information…'

Pro forma financial information

We would not normally expect to see pro forma financial information included in a circular where a listed offeror does not have access to the relevant offeree information. This is because it is not normally possible for the reporting accountants to confirm, as required by PR Appendix 3 Annex 2 item 7(b) (as applied by LR 13.3.3R) that the information is compiled on a consistent basis with the accounting policies of the issuer. In these cases, we would expect that LR 13.4.1R(5) is addressed via a narrative description covering the expected effect of the takeover or merger on the earnings or assets and liabilities of the group rather than through the use of pro forma financial information.

Working capital

LR 13.4.3R(3) permits the working capital statement in a circular to be presented on the basis of the listed offeror only, rather than the combined group, in a hostile or limited access situation. ~~In usual circumstances, access to the offeree's records and management is granted after the offer becomes unconditional, and we treat 28 days as sufficient time for advisers to complete the work necessary to provide relevant combined group information. Therefore, LR 13.4.3(3) states that the combined working capital statement should be included in the '28-day circular' discussed above.~~

~~Since this 28-day circular may be published after the listing of relevant securities (in most cases, offeror consideration shares), we require the original circular to say the working capital will be available on a combined basis as soon as possible.~~

[1] Following the changes made in CP12/25, the issuer will also be required to take responsibility. See LR 13.4.1R(4).

Revised offers

Finally, we come to hostile or contested bid situations where shareholders have approved the original terms of the offer. If the offer terms are revised or consideration increased, LR 10.5.2R may require further shareholder approval if the revision or increase is material. If this occurs before the date of the general meeting, LR 10.5.4R may require a supplementary circular. We encourage the offeror's sponsors to contact us as soon as possible to discuss the circumstances in this situation.

Similarly, where a previously non-recommended offer becomes recommended – or where access to information is granted – please consult us as soon as possible to discuss timetable implications for approving the documents and what additional requirements will apply.

Prospectuses

The following items cover some of the typical issues we encounter in hostile and limited access situations under the Prospectus Rules:

Working capital statements

PR Appendix 3 Annex 3 item 3.1, which requires the issuer to make a statement regarding the sufficiency of working capital for the next 12 months from the date of a prospectus, presents a particular difficulty where issuers have limited (or no) access to non-public information on offeree companies. This statement would take into account the impact of any material acquisition by the issuer.

The ESMA update of the CESR recommendations (ESMA recommendations) state clearly that a working capital statement in a prospectus must be 'clean' or 'qualified' and the decision is 'binary'. In coming to a clean statement, paragraph 115 of the ESMA recommendations does not permit issuers to disclose in a prospectus any assumptions, sensitivities, risk factors or caveats to the statement. This is because adding such disclosures detracts from the value of the statement and, in effect, seeks to transfer risk to investors.

In making a working capital statement, issuers are required to take into account a wide range of variables and sensitivities that may affect an issuer's working capital over the following 12-18 months. This analysis also involves taking into account the impact of any material acquisitions.

In some hostile takeovers, offerors will be able to come to a clean working capital statement in compliance with paragraph 115 of the ESMA recommendations after following procedures normally used to support this confirmation, even though no access to non-public information on the offeree is given to offerors and their advisers. This will be possible because such an offeror will have comfortable financing headroom that can be used to support a clean statement, even though they cannot fully assess the offeree's current and future working capital requirements.

However, in other hostile takeovers, undertaking the normal procedures to support a clean confirmation on the sufficiency of working capital is not generally possible due to the limited access to information on the offeree. It has been brought to our attention that, in these cases, offerors cannot make a qualified statement confirming the offeror does not have sufficient working capital either. This is because an offeror will not know the underlying working capital position of the offeree, so this statement is potentially misleading.

Having considered this matter internally, we intend to take a purposive approach to the application of the Prospectus Directive (PD) in these circumstances, concluding that an offeror may either:

- Include a clean or qualified working capital statement complying strictly with the ESMA recommendations.

- State that the offeror is not able to undertake appropriate procedures to support a statement on the sufficiency of its working capital, when taking into account the acquisition. The reason for this must be given, i.e. the offeror does not have access to non-public information on the offeree that allows those procedures to be undertaken. Offerors would then be required to give a 12-month working capital statement on the offeror on an unenlarged group basis. It must be clear from this statement that the acquisition has not been taken into account. We would expect the prospectus to state that if the offeror is granted access by the offeree before the close of the offer and access is sufficient for the purpose of making an enlarged group statement, the offeror will produce a supplementary prospectus containing an updated enlarged group working capital statement.

Pro forma financial information

As with our view on class 1 circulars, we would not normally expect to see pro forma financial information included in a prospectus where an offeror does not have access to the relevant offeree information. Once again, this is because it is not normally possible for the reporting accountants to confirm, as required by of PR Appendix 3 Annex 2 item 7(b) that the information is compiled on a consistent basis with the accounting policies of the issuer. In these cases, we would expect PR Appendix 3 Annex 1 item 20.2 to be addressed via a narrative description covering the expected effect of the takeover or merger on the earnings or assets and liabilities of the group, rather than through the use of pro forma financial information.

Responsibility statement

As per PR 5.5.3R, the directors and the company are required to take responsibility for the whole prospectus. This includes taking responsibility for information sourced from third parties. The PD does not provide for split-responsibility statements or any type of carve-out of responsibility. As such, the responsibility statement should track the wording PR Appendix 3 Annex 1 item 1.2 and Annex 3 item 1.2 and should not be modified to limit responsibility. In addition, issuers should be mindful of not including other disclosure in the document, which could be seen to qualify the responsibility statement.

Third party information

As with the responsibility statement, the PR Appendix 3 Annex 1 item 23.2 wording regarding the reproduction of third party information should track the rule's wording. Issuers should be careful not to modify the wording to imply they are limiting or qualifying the responsibility statement.

Risk factors

It is common in these types of documents for issuers to include a risk factor relating to the limited access situation. In reviewing risk factors, our primary concern would be to ensure that the risk factor does not limit responsibility. An example of the type of wording that issuers have previously included in a limited access situation is:

‘The issuer and its advisers have not had access to the target’s information or documentation and have been unable to perform any due diligence on such information or documentation. The information in relation to the target has been sourced from publicly available information and has not been subject to comment or verification by the target or the issuer or their respective directors. Nothing in this risk factor limits or qualifies the issuer or the directors’ responsibility under PR 5.5 or Part 6 FSMA.’

Information on the target

Section 87A(2) FSMA requires that all ‘necessary information’ is included within the prospectus or equivalent document. In deciding whether target information should be included, issuers should take into account the specific factors, such as the relative size of the target to the issuer and circumstances surrounding the transaction, as well as the level of publicly available information. As such, we would urge any advisers or issuers preparing a prospectus in a limited access situation to contact us as early as possible to discuss the exact disclosure requirements.

As part of the vetting process, we will ask the issuer to confirm to us that they consider the information included within the document is sufficient to meet the disclosure requirements under the PD and section 87A(2) FSMA. Unless the issuer is happy that these tests have been met, we will not be in a position to approve the prospectus.

Access granted

If an issuer is granted access and the offer is still open, issuers tend to consider this to be a significant new factor, requiring the production of a supplementary prospectus (SP). The SP should include, where relevant, additional information on the target and the enlarged group (such as the enlarged working capital statement).

UKLA Technical Note

Share buybacks – novel/complex approaches and Premium Listing Principle 5

Ref: UKLA / TN / 310.1

LR 2.2.4R, LR 7.2.1AR and LR 12.4

There are a number of approaches that can be used by premium listed issuers which achieve the same effect of a buyback of premium listed shares in substance but which are not a buyback of shares in legal form. In such circumstances, LR 12.4.10G advises that issuers should contact the FCA to discuss the application of LR 12.4 to their proposed transaction. Generally, where the method proposed replicates the substance of a share buyback, our approach is to interpret the rules purposively and apply LR 12 in a 'substance over form' manner.

A typical example is the return of value to shareholders involving the creation, issue and repurchase of a new class of shares followed by a share consolidation. Often such an approach also includes an income option through a special dividend as an alternative. We consider this method is acceptable where an issuer can demonstrate to us that an appropriate approach has been taken to apply the principles of LR 12.4 – for example, allowing all shareholders the ability to participate on the same terms where the substance of the transaction is equivalent to a buyback of over 15% of the issuer's shares occurring. However, where this (or a similar) method involves the 'stapling' of the new security to the existing equity share for a prolonged period of time, we would question the extent to which the premium listed equity shares remain freely transferable in their own right, as required under LR 2.2.4R. Issuers or their advisers proposing such approaches are recommended to contact us for individual guidance before embarking on this course (see below).

Equality of treatment in share buybacks

Premium listed issuers and their advisers are reminded that the principle of equality of treatment of shareholders applies to share buybacks. In summary, Premium Listing Principle 5 (LR 7.2.1AR) states that all shareholders that are in the same position must be treated equally. We will examine closely share buybacks undertaken in a manner that may offend this principle.

Some examples of share buybacks that we consider as potentially offending this principle are those that seek to:

- offer different terms to different shareholders (or groups of shareholders) without ~~apparent good reason~~a sound objective rationale for such shareholders to be viewed as being in a different position; ~~and~~or

- exclude certain shareholders (or groups ~~thereof~~of shareholders) ~~on a basis that is~~ without a sound objective rationale, for example the exclusion of shareholders in certain jurisdictions where it is not obvious that there is any sound reason to do so.

An example of a rationale that we would consider to be sound and objective would be where local laws or regulations in a particular jurisdiction may result in a significant risk of civil, regulatory or criminal exposure for the listed company if the buyback was conducted there. An example of a rationale that we would consider to be neither sound nor objective would be a buyback where shareholders in certain jurisdictions are excluded based on an apparent risk of such exposure but yet employees in the same jurisdiction have been included in the buyback and there is no basis for different treatment of employees/shareholders under the relevant local law or regulation. Similarly, an arbitrary size criterion for exclusion does not appear to present a sound objective rationale.

Contacting the FCA for individual guidance

Please note that the examples given above regarding what the FCA would consider to be a sound objective rationale (or otherwise) are not an exhaustive list. Where issuers and their advisers have queries over the correct application of the Listing Rules to their specific circumstances, they are encouraged to contact the FCA for individual guidance.

The procedure for requesting individual guidance is set out in SUP 9 of the FCA Handbook.

UKLA Technical Note

Disclosure of 'lock-up' agreements

Ref: UKLA / TN / 522.1

LR 1.3.3R, PR Appendix 3 Annex 3 item 7.3 and DTR 1.3.4R

Investors with a significant equity holding in a company may enter into lock-up agreements with their brokers for a certain period of time. This may occur at IPO or following a secondary market placing. Normally, investors who are party to such agreements are under an obligation to their broker not to sell their shareholding for a certain period of time, save in certain limited circumstances. However, on occasions, such commitments can also be waived, cancelled or modified before the end of the term of the lock-up agreement with the consent of the broker.

Listed companies themselves, both in respect of their own shares and as investors in other companies, can be subject to the obligations imposed by lock-up agreements and should consider their disclosure obligations in such circumstances. (Listed companies may, on occasion, also make disclosures on behalf of their significant investors.)

DTR 1.3.4R and LR 1.3.3R require, among other things, issuers to take reasonable care that information it notifies to a RIS or makes available through the FCA is 'not misleading, false or deceptive and does not omit anything likely to affect the import of the information'.

We would consider terms or conditions of a particular lock-up agreement which allow for a lock-up commitment to be modified, waived or cancelled by a party to the arrangement during the lock-up period to be relevant information within the scope of DTR 1.3.4R and LR 1.3.3R. Depending on the way the lock-up agreement is explained, the market may conclude, in the absence of such disclosure, that the relevant agreement~~s~~ ~~are~~is irrevocable~~ or unconditional~~. Therefore, we would expect listed companies to ~~give consideration to the disclosure of these terms or conditions~~provide sufficient clarity on this point when information regarding lock-up agreements is being announced or published.

Similarly, for transactions to which the Prospectus Rules apply, such as IPOs, explicit disclosure requirements exist in respect of the share securities note in the prospectus in relation to lock-up agreements (item 7.3 of Annex 3 in Appendix 3 of the Prospectus Rules). This requirement specifically mandates disclosure of the ‘content and exceptions of the agreement’ and an ‘indication of the period of the lock up’.

UKLA Technical Note

Pro forma financial information

Ref: UKLA / TN / 633.1

LR 13.4.1R(5), PR 2.3.1, PR Appendix 3 and ESMA Q&A 50, 51 and 54

Annex 1 item 20.2 of Appendix 3 of the Prospectus Rules requires, in the case of a **significant gross change**, a description of how the transaction might have affected the assets and liabilities and earnings of the issuer, had the transaction been undertaken at the commencement of the period being reported on or at the date reported.[1] The requirement will normally be satisfied by the inclusion of **pro forma financial information**, the presentation and content of which is set out in Annex 2 of PR Appendix 3.

What is a 'significant gross change'?

Article 4a(6) and Recital 9 of the PD Regulation (reproduced at PR 2.3.1) define a significant gross change as a variation of more than 25%, relative to one or more indicators of the size of the issuer's business, in the situation of an issuer due to a particular transaction, with the exception of those situations where merger accounting is required. Accordingly, if a prospectus is prepared in connection with a class 1 transaction by a premium listed issuer, there is a significant gross change. Similarly, a prospectus for a standard listed (or unlisted) issuer to raise funds for an acquisition that would have been classified as class 1 if the issuer had been premium listed would need to address the significant gross change.

While a significant gross change could be directly related to the production of the prospectus, this is not necessarily the case.

A significant gross change may result from a transaction which is not, in itself, the subject of the prospectus.

[1] Such requirement is also triggered by Annex 23 item 15.2 and Annex 25 item 20.2 of PR Appendix 3. For ease of reference, only Annex 1 item 20.2 will be mentioned for the purpose of discussion in this note.

A significant gross change transaction also covers situations where the transaction has not yet taken place but where the issuer has made a 'significant firm commitment' (ESMA Q&A 50 Aa). Despite the differing terminology, the effect of Article 4a(5) of the PD Regulation is that 'significant financial commitment' is the same thing as a 'significant firm commitment'.

We would consider that a pure fundraising transaction (eg, a large rights issue or an open offer~~ that is not undertaken in connection with an acquisition~~) would not constitute a significant gross change transaction for the purposes of Annex 1 item 20.2. However, if a fundraising is undertaken in connection with an acquisition, the related acquisition might, depending on its size, constitute a significant gross change.

What ~~is 'pro forma financial information'~~information does Annex 2 apply to?

For the purposes of identifying information in a prospectus to which the requirements of Annex 2 must apply, put simply, ~~I~~it is any information ~~represented by~~which includes a figure c ~~in the following~~which has been calculated by way of the formula '**a+b=c**' ~~formula~~, where:

- **a** is the historical financial information;
- **b** is the hypothetical adjustment (typically a transaction or change, for balance sheet purposes, that had not happened as at the date of **a** or, for income statement purposes, during the full period covered by **a**); and
- **c** is the resultant pro forma ~~financial~~ information.

Financial information where no hypothetical adjustment has been made (eg where it has simply been prepared on a different basis from the audited financial information) is not considered as being pro forma financial information for the purposes of Annex 2.

The requirement for a pro forma profit and loss account

Once a significant gross change has been identified, Annex 1 item 20.2 states that the prospectus must include:

'… a description of how the transaction might have affected the assets and liabilities and earnings of the issuer, had the transaction been undertaken at the commencement of the period being reported on or at the date reported.

This requirement will normally be satisfied by the inclusion of pro forma financial information.'

Annex 2 item 2 states that:

'In order to present pro forma financial information, a balance sheet and profit and loss account, and accompanying explanatory notes, depending on the circumstances may be included.'

We do not consider that Annex 2 should be regarded as mandating the production of any or all of these items of pro forma financial information, but rather as describing the way in which pro forma financial information should be presented and the information which must be included.

In ESMA Q&A 50 it is made clear that a narrative description of the impact on earnings or assets and liabilities will not *normally* be acceptable unless the inclusion of pro forma information:

- is not feasible (eg, if the issuer cannot gain access to the relevant information with reasonable effort, for example in a hostile takeover); or
- might not be a fair way to describe the effect of the transaction.

As such, we would expect a pro forma profit and loss account (P&L) to be presented in addition to a pro forma balance sheet and accompanying explanatory notes. In certain circumstances, a balance sheet and/or P&L may not be required if the impact of the significant gross change is already reflected in the issuer's published financial statements (as discussed further in ESMA Q&A 51).

'Voluntary' pro forma financial information – ie, where there is no significant gross change or where Annex 1 item 20.2 does not apply

When an issuer includes a pro forma balance sheet in a prospectus but there has not been a significant gross change for the purposes of Annex 1 item 20.2 (for example, ~~in the case of an IPO or a new top company, or for illustrative purposes to show how the proceeds of a rights issue will be allocated~~to illustrate the proceeds of an offering to be received by the issuer), we consider that this is not subject to Annex 1 item 20.2 because we consider this to be voluntary pro forma financial information. Similarly, if Annex 1 item 20.2 does not apply to an issue (for example, in the case of an issue of debt securities) then we would also consider any pro forma balance sheet included in the prospectus as being voluntary pro forma financial information.

We consider that this voluntary pro forma financial information would be subject only to the requirements of Annex 2 (as discussed in ESMA Q&A 54). Annex 1 dictates when an issuer must prepare pro forma financial information. Annex 2 explains how pro forma financial information should be presented and the information which must be included, whether as a consequence of being required by Annex 1 or due to being included voluntarily.

We consider that there is no requirement to include a pro forma P&L in circumstances where there is no significant gross change or where Annex 1 item 20.2 does not apply to the issuer.

However, for voluntary pro forma information presented by the issuer (regardless of whether it is a balance sheet or P&L), ESMA Q&A 54 requires such information to be prepared with the same level of care as when it is mandatory, and for it to be prepared and included in the prospectus following the requirements set out in Annex 2.

Class 1 circulars – effect on LR 13.4.1R(5)

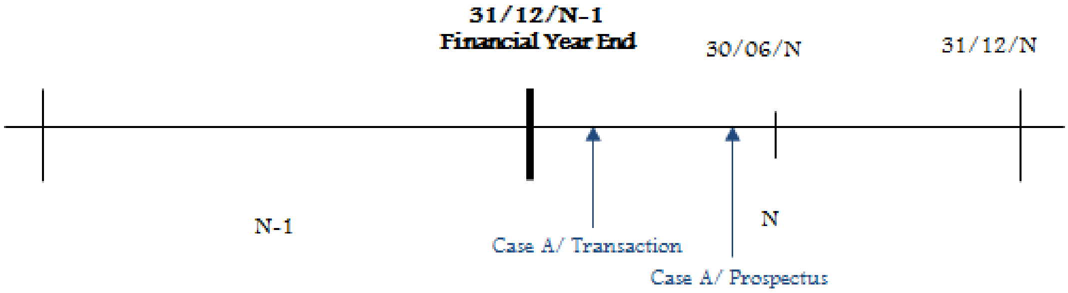
~~For class 1 circulars, we consider that the requirement in LR 13.4.1R(5) is similar in approach to Annex 1 item 20.2.~~

Market practice for class 1 circulars has been to include a pro forma balance sheet and a narrative statement on earnings. Notwithstanding the revised approach taken by ESMA with regard to significant gross changes for prospectuses, we would not expect this practice to change for class 1 circulars. However, we would highlight that if a prospectus is being produced in connection with the same transaction then, in relation to the prospectus, Annex 1 item 20.2 will apply in full.

Illustrative examples of pro forma P&L

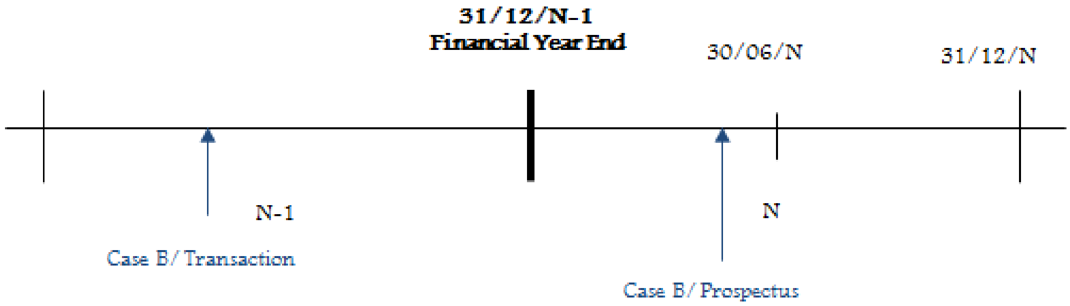
We illustrate below with two example cases. In both cases a prospectus subject to Annex 1 item 20.2 is being prepared in year N and one significant gross change has occurred which is not the trigger for the document (eg, the prospectus relates to a fundraising which is not, in itself, a significant gross change). The difference however is that in Case A the transaction resulting in the significant gross change is occurring in the financial year in which the prospectus is being prepared, whereas in Case B the transaction resulting in the significant gross change took place in the financial year prior to that in which the prospectus is being prepared.

Case A



In Case A, a pro forma P&L for the period ended 31 December N-1 would be required as if the transaction had happened on 1 January N-1, ie, the commencement of the period being reported, to reflect its impact on earnings for the full period. A pro forma balance sheet as at 31 December N-1 is also required to reflect the impact on assets and liabilities from the transaction at that date.

Case B



In Case B, a pro forma P&L for the period ended 31 December N-1 would be required as if the transaction had happened on 1 January N-1 as its impact on earnings has not been reflected for the full period. A pro forma balance sheet is not required as the impact on assets and liabilities from the transaction would have already been reflected in the balance sheet of the most recent completed financial statements (as at 31 December N-1).

The preparation of a pro forma P&L

As income statement information spans a period of time, a pro forma P&L needs to demonstrate the impact on earnings since the beginning of the financial period, whereas a pro forma balance sheet only needs to demonstrate the impact on assets and liabilities at the end of the financial period. Therefore, the preparation of a pro forma P&L can often be more complicated than that of a pro forma balance sheet.

In a Q&A format below, we address a number of issues that might be encountered in the preparation of a pro forma P&L.

1. *Should source financial information always appear in the prospectus?*

   Annex 2 item 3 states: 'The sources of the pro forma financial information have to be stated and, if applicable, the financial statements of the acquired businesses or entities must be included in the prospectus.'

   Therefore, if the acquired business has published financial statements then they will be required to be included in the document. In many cases the financial statements of the acquired business will already be part of the prospectus, having been included as a result of the complex financial history requirements as set out in Article 4a of the PD Regulation (reproduced in PR 2.3.1) or will otherwise be available, for example as part of the class 1 circular disclosures made by a premium listed company.

   Where there are no such financial statements that could be included in the prospectus then the "if applicable" test within Annex 2 item 3 would not be satisfied. This test should not be regarded as imposing a further requirement for the production of financial statements.

2. *Does the source financial information need to be audited?*

   There is no requirement resulting from Annex 2 itself for the source financial information to be audited.

   However, as noted above it is likely that, in certain situations where there has been a significant gross change, an issuer will ~~also~~have audited financial information available, for example as a result of the need to include additional financial information to meet the complex financial history requirements as set out in ~~PR 2.3.1~~ Article 4a of the PD Regulation (reproduced in PR 2.3.1). In particular, depending on the size of the acquired entity, the presence of audited source financial information for an adjustment may be sufficient to address the complex financial information requirements.

For example, in Case A above, where the 'significant gross change' transaction also occurred in year N, the complex financial history requirements could result in the inclusion of audited financial statements of the target(s) for year N-1 in the prospectus.

3. *If the target has no financial statements, would they need to be prepared specifically for the document?*

If financial statements are not available, we would accept the pro forma adjustments being sourced from unaudited financial information on the target(s), such as management accounts. We do not envisage requiring the production of financial statements purely for the purposes of the pro forma financial information.

It should be noted that, depending on size of the transaction, audited financial information may still need to be included in the prospectus for this period under the complex financial history provisions as discussed in 2, above.

4. *What approach ~~is best for a transaction which occurs~~may be taken in presenting a pro forma P&L for an acquisition that occurred in year N-1?*

For acquisitions such as Case B above, where the target's historical financial information was partially consolidated in the issuer's latest annual accounts, we consider that two alternative approaches could be used to demonstrate the impact on earnings.

Both approaches assume that the issuer's historical consolidated financial information (including the partially consolidated target information) is presented as the unadjusted information in the first column of the pro forma P&L.

We consider that the pro forma P&L could be prepared by:

(i) subtracting the partially consolidated target financial information and then adding the target's latest full year financial information to those of the issuer through separate adjustment columns of the pro forma P&L or

(ii) presenting the target financial information only for the pre-acquisition period in the adjustment column.

We would accept both approaches.

5. *Can the accounting exercise of purchase price allocations (PPAs) be viewed as 'factually supportable' and included as pro forma adjustments?~~ Can synergy benefits be viewed as 'factually supportable' and included as pro forma adjustments?~~*

The accounting exercise of purchase price allocation to ~~intangible~~ fixed assets at fair value and the subsequent amortisation or impairment of those ~~intangible~~ assets very often requires a degree of judgement and the use of assumptions.

We consider that PPAs are 'factually supportable' as required by Annex 2 item 6(c) and would expect to allow these as pro forma adjustments if the issuer:

- sets out in the explanatory notes ~~as transparently as possible~~ the basis adopted in making the PPAs;
- specifies any assumptions used; and
- where relevant, quotes ~~the~~any relevant supporting evidence~~, such as the Sale and Purchase Agreement~~.

Where a PPA is preliminary, we expect issuers to disclose this fact together with what events are expected to occur to complete the exercise and the potential impact of any re-allocation.

6. *Can synergy benefits be included as pro forma adjustments?*

By contrast, we consider that synergy benefits are ~~not sufficiently certain and are~~ dependent on future actions of management of the enlarged group after completion of the transaction. We consider that synergy benefits are not ~~'factually supportable'~~directly attributable to the transaction, as required by Annex 2 item 6(~~c~~b), and that accordingly they should not constitute pro forma adjustments.

~~6.~~7. *What is the time period that needs to be covered by pro forma financial information, in particular, would a six-month pro forma P&L be acceptable?*

ESMA stated through Q&A 51 that a period of six months is generally sufficient to describe how the transaction might have affected the earnings of the issuer. However, there may be situations where the time period should be longer, for example where the issuer's business is affected by seasonality. The decision about the time period should always include consideration of the circumstances on a case-by-case basis.

For example, if the prospectus in Case B above is being prepared in the second half of year N (rather than in the first half of year N) and the issuer has published its interim financial statements, no pro forma P&L would be necessary as the earnings impact of the transaction is already reflected in the interim financial statements for year N, unless in the circumstances of the case a longer time period would be required.

The report prepared by independent accountants

Any pro forma financial information included in a prospectus (whether or not there has been a significant gross change) must be prepared in accordance with Annex 2, including item 7. ESMA Q&A 54 is clear that this includes an accountant's report.

The typical SIR 4000 report used in the UK to report on pro forma financial information generally refers to the report being required by Annex 1 item 20.2. However, in the case of voluntary pro forma financial information, we consider that it is not appropriate to refer to this item, since this implies there has been a significant gross change. Instead, we consider that reference should be made to Annex 2 item 7 (the item which refers to an accountant's report).

Where historical financial information (annual or interim financial information) included in a prospectus itself includes pro forma financial information in order to comply with the applicable accounting framework (usually IFRS), we would not expect additional disclosure to be included to address Annex 2. However, if the pro forma financial information relates to a significant gross change, and Annex 1 applies to the issuer, then Annex 1 item 20.2 will need to be addressed.