

SEC Approves NYSE Proposal for Primary Direct Listings, Nasdaq Files Similar Proposal [Updated]

ALERTS

August 31, 2020

[Updated September 2, 2020: On August 31, the Council of Institutional Investors (CII) filed a [notice](#) with the SEC of its intent to petition for review of the SEC's order approving the NYSE's revised proposal to allow primary direct listings. On the same date, the SEC [notified](#) the NYSE of its receipt of this notice, and that the SEC's order approving the NYSE's revised proposal is now stayed until the SEC orders otherwise.]

On August 26, 2020, the U.S. Securities and Exchange Commission (SEC) [approved](#) the [revised proposal](#) filed by the New York Stock Exchange (NYSE) allowing companies to sell shares on their own behalf in direct listings. Previously, direct listings were limited to the sale of shares held by existing shareholders. The revised NYSE proposal, submitted in late June, details the procedures applicable to primary direct listing auctions on the NYSE, while also acknowledging and seeking to address potential Regulation M issues that may arise in primary direct listings.

The revised proposal was responsive to some of the concerns discussed in the SEC's [March 26 Order](#) relating to prior versions of the NYSE proposal (as have been discussed in our prior Alerts, [here](#) and [here](#)), including concerns related to: 1) the NYSE's proposed 90-trading day grace period to comply with the NYSE's initial listing distribution requirements to have at least 400 round-lot holders and 1.1 million publicly-held shares; 2) how the NYSE would be assured that a company would sell at least \$100 million in market value of shares in the opening auction on the first day of trading, and 3) how the NYSE's opening auction rules would apply in a primary direct listing and how it would "assure that the opening auction and subsequent trading promote fair and orderly markets, prevent manipulative acts and practices, protect investors, and otherwise would be consistent with Section 6(b)(5) and other relevant provisions of the [Securities Exchange Act of 1934]."

In addition to deleting the 90-trading day grace period discussed above, the NYSE's revised proposal clarified the NYSE's approach to primary direct listings, including by setting forth more detailed opening auction procedures.

The following is a summary of some of the key highlights of the amendments to the NYSE Listed Company Manual and the NYSE Rules as set forth in the NYSE's revised proposal, and as approved by the SEC:

- **Primary Direct Floor Listings - General.** The NYSE Listed Company Manual has been amended to allow a company to list its common stock on the NYSE at the time of effectiveness of a registration statement pursuant to which either 1) only the company itself is selling shares in the opening auction on the first day of trading or 2) the company itself and selling shareholders are selling shares in the opening auction, in either case, a "Primary Direct Floor Listing."

- Primary Direct Floor Listings - Market Value of Publicly-Held Shares Requirement. The NYSE Listed Company Manual has been amended to provide that a company undertaking a Primary Direct Floor Listing would be deemed to have met the applicable aggregate market value of publicly-held shares requirement for initial listing on the NYSE if either:
 - the company sells at least \$100 million in market value of shares in the opening auction on the first day of trading on the NYSE; or
 - where the company sells less than \$100 million in market value of shares in the opening auction on the first day of trading on the NYSE, the company's aggregate market value of the shares 1) that are sold in the opening auction on the first day of trading and 2) that are publicly held immediately prior to listing, is at least \$250 million, with market value calculated using a price per share equal to the lowest price of the price range set forth by the company in its registration statement.

In its revised proposal, the NYSE noted that officers, directors, and owners of more than 10 percent of the company's common stock could purchase shares sold by the company in the opening auction, purchase shares sold by other shareholders, or sell their own shares in the opening auction and in trading after the opening auction "to the extent not inconsistent with general anti-manipulation provisions, Regulation M, and other applicable securities laws." In addition, while shares held by these persons are not included in the calculation of publicly-held shares for purposes of the NYSE listing rules, the NYSE noted that these persons "may acquire in secondary market trades shares sold by the issuer in a Primary Direct Floor Listing that were included when calculating whether the issuer meets the market value of publicly-held shares initial listing requirement."

The NYSE further advised that companies listing on the NYSE in connection with a Primary Direct Floor Listing or a Selling Shareholder Direct Listing would still be required to meet all other applicable listing requirements of the NYSE, including the requirements to have at least 400 round-lot holders and 1.1 million publicly-held shares.

- Primary Direct Floor Listings - Auction Procedures. The NYSE Rules have been amended to set forth the procedures for a Direct Listing Auction¹ that are to be used for a Primary Direct Floor Listing, which would, among other things, assure that a company has sold the necessary market value of shares in the opening auction.
 - New Primary Direct Listing Order. The NYSE has added a new type of order for Primary Direct Floor Listings, referred to as an Issuer Direct Offering Order (IDO Order). Companies that undertake Primary Direct Floor Listings are required to use an IDO Order, which is a limit order to sell shares in a Direct Listing Auction. The requirements of an IDO Order are as follows:

"(i) only one IDO Order may be entered on behalf of the issuer and only by one member organization;

(ii) the limit price of the IDO Order must be equal to the lowest price of the price range established by the issuer in its effective registration statement ("Primary Direct Floor Listing Auction Price Range");

(iii) the IDO Order must be for the quantity of shares offered by the issuer, as disclosed in the prospectus in the effective registration statement;

(iv) an IDO order may not be cancelled or modified; and

(v) an IDO Order must be executed in full in the Direct Listing Auction."

These requirements are intended, at least in part, to provide certainty that the number of shares disclosed in the company's effective registration statement will be sold in the Direct Listing Auction and will be priced within the range specified in the effective registration statement. If the IDO Order is not executed in full, then the Primary Direct Floor Listing would not be able to proceed, and the shares would not begin trading on the NYSE.

- DMM Responsibilities. As has been the case with respect to Selling Shareholder Direct Floor Listings, a Direct Listing Auction for a Primary Direct Floor Listing is required to be conducted manually (rather than electronically) by a Designated Market Maker, or DMM. The NYSE Rules have been amended to specify the DMM responsibilities in Primary Direct Floor Listings including, among other things, rules relating to the DMM's determination of the indication reference price, the auction price, and allocation and participation in the Direct Listing Auction.

In addition, the DMM is not permitted to conduct a Direct Listing Auction for a Primary Direct Floor Listing if 1) the auction price is outside of the price range set forth in the company's effective registration statement or 2) there is insufficient interest to satisfy the IDO Order and all better-priced sell orders in full.

In effect, these amendments "make the DMM responsible for determining whether the Direct Listing Auction can proceed." If the Direct Listing Auction is unable to proceed, then the NYSE will "notify market participants via Trader Update that the Primary Direct Floor Listing has been cancelled and any orders for that security that have been entered on the Exchange, including the IDO Order, would be cancelled back to the entering firms."

The NYSE also added commentary to this Rule providing that when the DMM consults with a financial advisor, whether in a Selling Shareholder Direct Floor Listing or in a Primary Direct Floor Listing, as to pricing or opening of trading, "the financial advisor and DMM will not act inconsistent with Regulation M, and other anti-manipulation provisions of the federal securities laws, or Exchange Rule 2020." In addition, the NYSE noted that it "has retained the Financial Industry Regulatory Authority, Inc. (FINRA) pursuant to a regulatory services agreement to monitor such compliance...."

Nasdaq Files Primary Direct Listing Proposal

On August 24, 2020, the Nasdaq Stock Market filed a similar [proposal](#) with the SEC to allow companies to sell shares on their own behalf in direct listings. The proposal contemplates the creation of a new order similar to the NYSE's IDO Order, referred to as a Company Direct Listing Order (CDL Order).

There are several differences between the Nasdaq proposal and the final NYSE amendments including, among others: 1) a company will be deemed to have satisfied the market value of unrestricted publicly held shares initial listing requirement if its unrestricted publicly held shares before the offering (calculated using a price per share equal to 20 percent below the lowest price of the price range in the registration statement) *plus* the market value of the shares to be sold in the opening auction is at least \$110 million (or \$100 million, if the company has stockholders' equity of at least \$110 million); 2) the CDL Order is a "market order" that must be entered *without a price*, whereas the NYSE's IDO Order is a "limit order" that must be entered with a price limit equal to the lowest price of the price range in the registration statement; and 3) the shares will not be released for trading by Nasdaq unless the shares are able to be sold at or above a price that is 20 percent below the lowest price of the price range set forth in the registration statement.

We are continuing to monitor developments relating to primary direct listings on the Nasdaq Stock Market.

What to Do Now?

These amendments to the NYSE Listed Company Manual and the NYSE Rules are effective now, providing yet another avenue for companies to offer and sell their shares in the public markets. While the number of companies able to undertake a direct listing may remain limited due to, among other things, the NYSE's initial listing requirements (including the requirement that companies must have at least 400 round-lot holders), the ability for companies to raise capital in primary direct listings will likely result in more companies considering this pathway to going public.

Among other things, companies considering a primary or secondary direct listing may want to review their existing investment documents, including their investors' rights agreement and equity plan agreements, or any debt agreements, to determine whether those agreements accommodate a direct listing or only accommodate a traditional underwritten initial public offering, as some of those agreements may need to be amended in advance of the completion of the direct listing.

For more information about direct listings or any related matter, please contact any member of Wilson Sonsini's [capital markets](#) practice.

[1] NYSE Rule 7.35(a)(1)(E) defines "Direct Listing Auction" as the Core Open Auction for the first day of trading on the Exchange of a security that is a Direct Listing.