



## PSX RESPONSE PAPER

[With reference to PSX Notice No. PSX/N-118 dated January 27, 2021]

*Proposed amendments to PSX Regulations in relation to introduction of regulatory framework governing Direct Listing of companies at PSX*

August 05, 2021

### 1. INTRODUCTION:

- 1.1 PSX publishes 'Response Paper' on its website after close of consultation process on proposed amendments to PSX Regulations. The Response Paper sets out PSX's response to the comments received on the proposed regulatory amendments.
- 1.2 PSX vide notice No. PSX/N-118 dated January 27, 2021 invited public to submit their comments and feedback on proposed amendments to PSX Regulations in relation to introduction of regulatory framework governing Direct Listing of companies at PSX, latest by February 02, 2021.

**Note:** For details on the above notice, readers may peruse the same by clicking the following link:

<https://www.psx.com.pk/psx/resources-and-tools/listings/public-comments>

- 1.3 PSX received comments from only two respondents who consented to reveal their identity along with comments. PSX is thankful to the respondents for submitting comments.

S. #	Respondent's Name	Designation	Company
1.	Syed Mustafa Zamin	Senior Associate, Corporate Finance & Advisory	Topline Securities Limited (TSL)
2.	Hammad Ali Faisal	Chief Compliance Officer	Central Depository Company of Pakistan Limited (CDCPL)

- 1.4 Comments received from **TSL** along with responses of PSX are mentioned below:

S. #	PUBLIC COMMENTS	RESPONSE OF PSX
(i)	Having studied the draft amendments, we feel that the purpose of this amendment is unclear and we are struggling to surmise the potential benefits of the proposed amendment. For this purpose, we would like to request the PSX to arrange an interactive session whereby this particular methodology of listing can be discussed in depth and the respected personnel of this industry be apprised on the potential bearing on the Pakistan Stock Exchange.	Direct Listing have increasingly been gaining attention as a means for a private company to go public.  A Direct Listing refers to the listing of a private company on the Exchange usually without appointment of intermediaries.  Direct Listing would provide companies with a quick and easy route to list on the Exchange.



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	<p>Further, having studied the regional regulations concerning Direct Listings, we have been able to understand that Direct Listings are mostly allowed in cases where,</p> <ol style="list-style-type: none"> <li>1. Applicants are already listed at one exchange; Direct Listings are used to facilitate time efficiency;</li> <li>2. Where the APEX Corporate Regulator is enforcing a Company to list at the Stock Exchange.</li> </ol>	<p>A Direct Listing would also provide a company with many of the benefits of a traditional IPO, including access to the public markets for capital raising.</p> <p><b>Benefits:</b></p> <ul style="list-style-type: none"> <li>• Lower listing costs;</li> <li>• No mandatory requirement of appointment of underwriters;</li> <li>• Optional requirement of appointment of a Financial Adviser.</li> <li>• Subsequent to Direct Listing, a company would be able to avail benefits available to listed companies, such as bank borrowing at attractive rates (lower spread).</li> </ul> <p>Direct Listing practices differ from jurisdiction to jurisdiction, for example:</p> <ul style="list-style-type: none"> <li>• In Canada, a company already listed on another exchange may list directly on TSX or TSXV.</li> <li>• In Singapore, Direct Listing framework is only applicable on Chinese companies incorporated in China.</li> <li>• In Saudi Arabia, Direct Listing is only allowed on Nomu, which is a parallel equity market with lighter listing requirements that serves as an alternative platform for growing companies that do not yet meet the requirements for the Main Market and look to raise capital and access the capital markets.</li> <li>• In Turkey, the issue document of all Direct Listing applicants is approved by the apex regulator (i.e. CMB), and shares of companies directly listed are traded on the EMQI (Equity Market for Qualified Investors).</li> </ul>



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	<p>Furthermore, we would like to document our concerns regarding (a) the absence of price discovery in this process (b) limited float of the stocks directly listed resulting in dearth of trading and activity (c) potential for price manipulation where only a few investors are trading between themselves.</p>	<p>These concerns have been addressed by introducing criteria for determination of opening price of a Direct Listing.</p> <p>Kindly refer to clause 5D.7 of PSX Regulations which specifies opening price determination for three (3) types of Direct Listings:</p> <ul style="list-style-type: none"> <li>(i) Direct Listing involving Accredited Investors;</li> <li>(ii) Direct Listing involving exiting shareholders; and</li> <li>(iii) Direct Listing involving specific category of investors.</li> </ul> <p>Moreover, with respect to Direct Listing involving Accredited Investors, the companies directly listing would be required to maintain a minimum level of free float as mentioned below as per clause 5D.3.1 (h) of PSX Regulations:</p> <table border="1" data-bbox="922 1100 1406 1352"> <thead> <tr> <th>Paid-Up Capital</th> <th>Free Float</th> </tr> </thead> <tbody> <tr> <td>Upto to Rs. 2.5 billion</td> <td>15%</td> </tr> <tr> <td>Above Rs. 2.5 billion and up to Rs. 5 billion</td> <td>10%</td> </tr> <tr> <td>Above Rs. 5 billion and up to Rs. 10 billion</td> <td>5%</td> </tr> <tr> <td>Above Rs. 10 billion</td> <td>2.5%</td> </tr> </tbody> </table>	Paid-Up Capital	Free Float	Upto to Rs. 2.5 billion	15%	Above Rs. 2.5 billion and up to Rs. 5 billion	10%	Above Rs. 5 billion and up to Rs. 10 billion	5%	Above Rs. 10 billion	2.5%
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	<p>Kindly find below further section wise comments by TSL on the proposed amendments.</p>											
(ii)	<p>It is our opinion, that the quality of listed companies will get affected. This is due to the fact that mostly companies in Pakistan do not possess expertise required to evaluate intricacies involved pre and post listing. This may also lead to a scenario whereby not only the transparency but the quality of issues could get compromised in the absence of necessary and proper due diligence that is customary in the event of bringing a new company to the bourse.</p> <p>Processes such as Due Diligence, guidance on Corporate Governance, drafting of marketing documents and pricing of the</p>	<p>Your kind attention is invited to PSX Regulation 5D.5.1, which states that:</p> <p><i>The company may appoint a Financial Advisor through an agreement in writing, at-least till the date of its Direct Listing.</i></p> <p><i>Provided that the Exchange reserves the right to require an applicant company to appoint a Financial Advisor if it deems appropriate in the interests of the investors and the market at large.</i></p> <p><i>Provided further that in case of Direct Listing involving specific category of</i></p>										



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	<p>company's shares are specialized tasks that expertise and diligence.</p>	<p><i>investors (defined at 5D.2.1. (b) above), appointment of Financial Advisor is mandatory, if two Market Makers are not appointed.</i></p> <p>Hence, you would agree that the PSX Regulations have been given adequate coverage with respect to appointment of Financial Advisor.</p>
(iii)	<p>In our opinion, the preparation of marketing documents such as the Information Memorandum and specialized investor presentations require expertise which most unlisted corporates do not possess. Furthermore, the entire preparation phase is utilized by Companies as well as Intermediates to ensure that the guidance is provided to the Companies on all aspects pre and post listing including matters of corporate governance, financial reporting, disclosures, etc. Therefore, simply compiling an Information Memorandum should not be treated as the sole basis of listing.</p>	<p>PSX agrees with this comment and has accordingly updated the PSX Regulations.</p> <p>Your kind attention is invited to PSX Regulation 5D.5.2, which states that the Financial Advisor shall perform such duties and functions as may be assigned to it by the company, which may include the following:</p> <ul style="list-style-type: none"> <li>(a) To assist the company in drafting the Information Memorandum;</li> <li>(b) To submit Direct Listing application to Exchange on behalf of company;</li> <li>(c) To ensure that the reference price or floor price in case of Direct Listing involving Accredited Investors is determined accurately, transparently and fairly.</li> </ul>
(iv)	<p>We believe that the role of Consultant to the issue should be mandatory and entrusting the Issuers to undertake the assignment themselves may lead to compromise in terms of quality of Companies trading on the Exchange given that the Companies are allowed a 2-year grace period to meet the requirements of Code of Corporate Governance. The role of a Consultant not only encompasses documentation but also educating the issuers with their Corporate Governance, matters of financial reporting, disclosures as well as improvements in their corporate as well as reporting structures. This is a specialized role which requires expertise not only with regards to development of official legal documents such as the Information memorandum / Prospectus In</p>	<p>Please refer to our comments given in serial no. (ii) and (iii) above.</p> <p>Moreover, with respect to their comment pertaining to allowing a 2 year grace period for companies directly listed at PSX to meet the requirements of Code of Corporate Governance, PSX has accordingly updated the Chapter 5D to make Listed Companies (Code of Corporate Governance) Regulations, 2019 applicable from the date of Direct Listing.</p>



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	this case and specialized presentations, but also, marketing & placement expertise.	
(v)	The Criteria given for opening price whereby lowest of the (i) Book Value (ii) Earnings Multiple based price (iii) Comparative transactions based price may lead to very depressed pricing and not represent the fair value of the stock. Other methods to calculate the Fair value of the share should also be considered.	<p>PSX agrees with the comments. Accordingly, following changes have been incorporated:</p> <ul style="list-style-type: none"> <li>(i) In case of <b>Direct Listing involving Accredited Investors</b>, the reference price/ opening price will only be determined through Book Building process.</li> <li>(ii) In case of <b>Direct Listing involving existing shareholders</b>, where Financial Advisors have been appointed, the reference price/ opening price will be decided by the Financial Advisor in consultation with the Company.</li> <li>(iii) In case of <b>Direct Listing involving specific category of investors</b>, where Financial Advisors have been appointed, the reference price/ opening price can be decided by the Financial Advisor in consultation with the Company or be determined through Book Building process.</li> <li>(iv) In case of Direct Listing involving existing shareholders or specific category of investors, where Financial Advisors are not appointed, then reference price/ opening price shall be lowest of the following, to be calculated on the basis of the latest audited financial statements: <ul style="list-style-type: none"> <li>(a) Book value per share.</li> <li>(b) Relative valuation.</li> <li>(c) Average market price of private transactions held during last one year.</li> </ul> </li> </ul>
(vi)	It is our opinion that strict compliance with the Code of Corporate Governance should be identical to practice required in case of a normal listing at the Exchange.	PSX agrees with this comment and has accordingly updated Chapter 5D of PSX Regulations to make Listed Companies (Code of Corporate Governance) Regulations, 2019 applicable from the date of Direct Listing.



1.5. Comments received from **CDCPL** along with responses of PSX are mentioned below:

S. #	COMMENTS	RESPONSE OF PSX
(i)	<p>While proposed amendments eliminates the procedure of issuing of shares to the general public and ancillary requirements to issue statement of lieu of prospectus.</p> <p>We feel it is important to refer the definition of the term “offeror” and “private offering (non-public offering) or private placement” read with section 87(2) and 87(5). As per the proposed Regulations, Offeror shall issue an Information Memorandum for the Accredited Investors which will be published for inviting their offers.</p> <p>Accordingly, Financial Advisor will host an investor day to pitch the offer. In view of foregoing, we understand media is used for inviting offers which excludes it from the definition of private offering.</p> <p>Consequently, the exemption available under section 87(5) will not be available and Offeror will be required to issue prospectus/ statement in lieu of prospectus under section 87(2) of the Act.</p>	<p>We don't agree with this comment. Due to private placement nature of Direct Listing, general public is not allowed to trade in shares of a company being listed directly. Instead, a class of investors which meet the minimum criteria can trade in those securities.</p> <p>Our understating is that only Accredited Investor would participate in investor day.</p> <p>However, to avoid confusion, PSX has agreed to remove proposed clause 5D.5.2 (b) as notified by PSX vide Notice no. PSX/N-118 dated January 27, 2021.</p>
(ii)	<p>We understand Securities Broker (either on their own or with support of PSX) will be ensuring that only eligible persons are placing trade orders for securities directly listed/ privately placed debt securities or on GEM Board.</p>	<p>This understanding is correct.</p>
(iii)	<p>The term “Accredited” is defined in the Securities Act, 2015 which means accredited in accordance with section 67. Therefore, the term “Accredited Person” shall be renamed in light of Act.</p>	<p>We understand that the referred term defined in Securities Act is different in nature, functions and purpose than the term defined in Chapter 5D.</p>
(iv)	<p>We understand the functions of “Financial Advisors” seems related to the functions of “Securities Advisors” which is a Regulated Activities under the Securities Act, 2015. Therefore, the term shall be renamed and only licensed person shall be permitted to perform such activity as per section 64 of the Act.</p>	<p>The role of Securities Advisors, which are required to be licensed under the Securities and Futures Advisers (Licensing and Operations) Regulations, 2017 is different from the role of Financial Advisor under the Direct Listing framework.</p>



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		The Financial Advisors are not regulated and their functions can be decided mutually between the company and such advisor.
(v)	<p>1. How it will be ensured that promoters/ sponsors/ controlling directors/ majority shareholders hold 51% of the paid-up capital at all times during the restriction period? Relevant provisions in the Regulations shall be prescribed.</p> <p>2. We understand requirement to block the shares held by sponsors in the manner prescribed in the Regulation 5 of the Public Offering Regulations, 2017 will not be applicable.</p>	<p>CDC will block their shareholding on the advice of PSX.</p> <p>This understanding is correct. The Public Offering Regulations will not be triggered as the offer of shares is not made to the public at large, rather to a specific segment of public known as 'Accredited Investors'.</p>
(vi)	We understand "Accredited persons" will not be able to exercise "withdrawal of shares" option as envisaged under section 74 of the Companies Act, 2017.	Section 74 will apply on Accredited Investors.
(vii)	In order to promote good governance and protect stakeholder's interest, compliance with Code of Corporate Governance shall be mandatory from the date of Direct Listing.	PSX agrees with this comment and has accordingly updated the Chapter 5D of to make Listed Companies (Code of Corporate Governance) Regulations, 2019 applicable from the date of Direct Listing.
(viii)	<p>What will be the treatment in following scenario?</p> <p>1. Issuer fail to fulfill its obligations under the CDC Regulations. We suggest, PSX shall follow the procedures as are currently being followed if Issuer fails to comply PSX Regulations, which leads to shifting to defaulter counter, suspension and delisting.</p> <p>2. Treatment of securities delisted from PSX. How Issuer will be made accountable to provide physical share certificate due to delist by PSX and revocation by CDC as consequent action.</p>	As provided in PSX Rule 5D.1.2, all the provisions relating to post-listing requirements provided in Chapter 5 of PSX Regulations shall be applicable to companies directly listed on the Exchange.
(ix)	We understand any conditions imposed under any other law imposed on specialized entities like Modaraba Management Company etc. will remain intact and will be ensured meticulously in	This understanding is correct.



S. #	COMMENTS	RESPONSE OF PSX
	case of any contradiction with these Regulations.	
(x)	Declaration of CDS Eligibility shall be compulsory at the time of making an application.  Moreover, Direct Listing permission shall only be granted once 100% shares are inducted in the CDS.	Correct and the same has been stipulated in clause 5D.3.1 (k).
(xi)	The term “investor” where ever used shall be replaced with “Accredited Investors”.	Agreed. The term ‘investor’ has been replaced at appropriate places.
(xii)	Please clarify the treatment for movement of Direct Listed Securities in the CDS by way of Free Delivery for e.g. Gift to family/ non-family members, transmission, transfer by way of court etc.	Treatment will be similar as presently laid down in Section E [ <i>Authorization under Sections 12 and 24 of the CDC Act exclusively for settlement of underlying trades, pledge and recovery of payments, charges and losses (for Sub-Account Only)</i> ] of CRF for Individuals, prescribed in Chapter 4 of PSX Regulations.
(xiii)	What will happen after the completion of 5 years Compliance Period?  Moreover, will general public may purchase shares of Direct Listed Company after 5 years?	Initially, the retention period for promoters/ sponsors/ controlling directors/ majority shareholders to retain their shareholding, on a cumulative basis, equivalent to not less than 51% of the paid-up capital of company was proposed to be till 5 years from the date of Direct Listing.  As per the approved regulations, the retention period for above mentioned persons is till the time the company remains directly listed on the Exchange.  General public cannot trade in shares of a company directly listed at the Exchange.

## 2. IMPLEMENTAION OF PROPOSED AMENDMENTS:

The proposed amendments have taken effect from **May 28, 2021**.