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SEC Approves Nasdaq Rule Change to Facilitate Listing Without an Initial Public Offering

In February 2019, The Nasdaq Stock Market LLC (“Nasdaq”) filed notice with the SEC of a proposed rule change creating new Listing Rule IM-5315-1 (available [here](#); the text of the revised rule is available [here](#)) to the Nasdaq Global Select Market listing standards designed to facilitate a direct listing of a company’s shares without conducting an initial public offering. The SEC [approved](#) the proposed rule change, which became effective upon filing.

New Listing Rule IM-5315-1 is substantially similar to the direct listing rule adopted by the New York Stock Exchange (“NYSE”) in February 2018 (see our prior client alert [here](#)) and is aimed at facilitating direct listings by the growing number of highly valued start-ups, including so-called “unicorns,” that have tended to delay going public in part because they have sufficient capital and therefore have no need to raise additional capital by undertaking a traditional underwritten primary offering of their shares. Direct listings can be attractive for these companies since they avoid the underwriters’ discounts and commissions of a traditional IPO, prevent dilution of existing shareholders (as there would be no new issuance) and eliminate the contractual restrictions (lock-ups) on resales imposed by underwriters (though the securities law restrictions under Rule 144 are unaffected). In April 2018, Spotify Technology took advantage of the NYSE rule change to undertake a direct listing on the NYSE.

Listing on an Exchange

A company generally lists on a stock exchange as part of an underwritten IPO, in connection with a transfer from another market or secondary listing (following a listing on another, typically offshore, exchange) or as a result of a spin-off/demerger.

Prior to the rule change, a company that had not previously had its common equity securities registered under the Exchange Act could list on the Nasdaq Global Select Market without conducting an IPO, at the discretion of Nasdaq, if the value of its publicly held shares was at least \$110 million (or \$100 million, if the company had stockholders’ equity of at least \$110 million), based on the lesser of an independent third-party valuation of the company and the most recent trading price for the company’s common stock in a private placement market.

The new rule eliminates the requirement to have a private placement market trading price in order to list directly on Nasdaq in case of equity securities that had not sustained recent trading in a private placement market prior to listing. Instead, for any such security, Nasdaq may determine that a company has met the

market value of publicly held shares requirement if the company provides an independent, third-party valuation evidencing a market value of publicly held shares of at least \$250 million. The valuation must be provided by an entity that has significant experience and demonstrable competence in the area of valuations, and it must be of a recent date as of the time of the approval of the company's listing. Nasdaq will consider any market factors or company-specific factors if there is concern that the value of the company has diminished since the date of the valuation and will continue to monitor the appropriateness of relying on that valuation up to the time of listing. In proposing this change, Nasdaq expressed its view that the current requirement to rely on recent private placement market trading in addition to a valuation could cause difficulties for companies that are otherwise qualified for listing due to the fact that they do not have their securities traded on a private placement market prior to going public.

Under the new rule, a direct listing will additionally require the company to file a resale registration statement for its outstanding shares sold in earlier private placements, which will be subject to SEC review and comment. As with listings in connection with IPOs, companies undertaking a direct listing will be subject to restrictions on publicity and the liability provisions of the Securities Act.¹

Independence of Third Party Providing Valuation

The new rule establishes certain criteria that would preclude a valuation agent from being considered "independent." Specifically, a valuation agent will not be considered independent if:

- the valuation agent or any affiliated person or persons beneficially own in the aggregate as of the date of the valuation, more than 5% of the class of securities to be listed, including any right to receive any such securities exercisable within 60 days;
- the valuation agent or any affiliated entity has provided any investment banking services to the listing applicant within the 12 months preceding the date of the valuation; or
- the valuation agent or any affiliated entity has been engaged to provide investment banking services to the listing applicant in connection with the proposed listing or any related financings or other related transactions.

¹ This new rule only applies to companies listing on the Nasdaq Global Select Market. Nasdaq intends to file a proposed rule change in the future to adopt requirements for the Nasdaq Capital and Global Markets applicable to companies which have not been listed on a national securities exchange or traded in the over-the-counter market pursuant to FINRA Form 211 immediately prior to the initial pricing and wish to list their securities to allow existing shareholders to sell their shares and clarify the use of the so-called "IPO Cross" for initial pricing of such securities.

Foreign Exchange Listings; Role of Financial Advisor

For a company transferring from a foreign-regulated exchange where there is a broad, liquid market for the company's shares, or listing on Nasdaq while trading on such exchange, Nasdaq will determine that the company has met the applicable price-based requirements based on the recent trading in such market. The new rule clarifies that a company transferring from a foreign-regulated exchange where there is a broad, liquid market for the company's shares or listing on Nasdaq while trading on such exchange is not subject to the new requirements applicable to direct listings.

Nasdaq also amended Nasdaq Rule 4753 to clarify that for a security that has had recent sustained trading in a private placement market prior to listing, the opening price will be the most recent transaction price in that market. If there has not been recent sustained trading in a private placement market, the price will be determined by Nasdaq in consultation with the broker-dealer serving as a financial advisor to the company.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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