ICGN
International Corporate Governance Network
Inspiring good governance & stewardship

European Commission
Brussels, Belgium

Email feedback: EU Login (europa.eu)

28 March 2023

Dear Members of the European Commission,

Re: Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on multiple-vote share structures in companies that seek the admission to trading of their shares on an SME growth market

And

Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL amending Directive 2014/65/EU to make public capital markets in the Union more attractive for companies and to facilitate access to capital for small and medium-sized enterprises and repealing Directive 2001/34/EC

The International Corporate Governance Network (ICGN) appreciates the opportunity to comment on the final proposals noted above that are part of the Listing Act package, containing "a set of measures to make public capital markets more attractive for EU companies and facilitate access to capital for small and medium-sized companies (SMEs)".[1]

Established in 1995, ICGN's purpose is to convene capital market participants to develop, promote and embed high standards of corporate governance and investor stewardship worldwide to preserve and enhance long-term value, contributing to sustainable economies, societies, and the environment. ICGN Members, many of whom are investors responsible for assets of around $70 trillion, are based in over 40 countries - largely in Europe and North America, with growing representation in Asia. For more information visit www.icgn.org.

ICGN's work programme is guided by the ICGN Global Governance Principles[2] and the Global Stewardship Principles[3], both of which are developed in consultation with ICGN Members. The ICGN Global Governance Principles were referred to in the EU Corporate Sustainability Reporting Directive (recital 44) as an authoritative global framework of governance information of most relevance to users. Many ICGN Members refer to the ICGN Global Governance Principles in their corporate governance assessments, proxy voting policies and company engagements. The Principles also inform governments and regulatory agencies on internationally accepted standards to help inspire the evolution of national corporate governance codes.

With respect to the above consultations, please note our response below the proposed changes in bold:

[1] EU Listing Act - Multiple share classes proposal, p. 2.
[2] ICGN Global Governance Principles 2021
[3] ICGN Global Stewardship Principles 2020

RH.205, The Record Hall, 16-16A Baldwins Gardens, EC1N 7RJ
VAT No. 927 1665 09 | Registered in England No. 6467372
t: +44 (0)2045417255
e: membership@icgn.org
w: www.icgn.org
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Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on multiple vote share structures in companies that seek the admission to trading of their shares on an SME growth market.

On 22 February 2022, ICGN responded to the EU's consultation on the Listing Act: Making Public Capital Markets More Attractive for EU Companies and Facilitating Access to Capital for SMEs. ICGN responded to Questions 101-105, relating to shares with multiple voting rights and noted:

> *"ICGN is concerned by the 'race to the bottom' that is taking place in many markets globally, in which the relaxation of past multiple voting rights limitations is regarded as justified to attract market listings. Stock exchanges may benefit, the underwriting community may benefit and issuing companies may benefit. But at the expense of shareholder rights and investor protections.[4]"*

ICGN's position remains unchanged. We are particularly concerned with the language in Article 4 as follows:

> *"Member States shall ensure that companies that do not have shares that are admitted to trading on a trading venue have the right to adopt multiple-vote share structures for the admission to trading of shares on an SME growth market in one or more Member States. Member States shall not prevent the admission to trading of shares of a company on an SME growth market on the ground that the company has adopted a multiple-vote share structure."*[5]

Companies that wish to access public capital are subject to enhanced disclosure requirements and are held accountable by shareholders through the exercise of voting rights, company monitoring and engagement – otherwise known as 'stewardship' obligations. In doing so shareholders play an important role in promoting the long-term success of companies. We understand that Founder(s) and early investors may wish to retain a degree of control in an emerging public company to preserve their ability to influence its strategic direction. However, this should not be facilitated through the inequitable treatment of non-controlling shareholders. More specifically, unequal (multiple) voting structures may serve to entrench management and allow founder(s) and controlling shareholders to monopolize the decision-making and potentially put minority shareholder interests at risk.

The ICGN Global Governance Principles describe the importance of the equitable treatment of shareholders in relation to share structures under guidance point 9.1 as follows:

> *"Ordinary or common shares should feature one vote for each share. Divergence from a 'one-share, one-vote' standard (e.g., multiple vote shares) which gives certain shareholders power or control disproportionate to their economic interests should be avoided..."*[6]

ICGN furthermore recommends that:

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[4] ICGN's response to the 2020 Hill Review provides a detailed assessment of the shareholder perspective on multiple vote shares. 26. ICGN Letter to UK Hill - Call for Evidence – UK Listings Review

[5] EU Listing Act - Multiple share classes proposal, pp. 20-21.

[6] ICGN Global Governance Principles 2021, p. 33.

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- The Board should review the company's share structure on an annual basis.

- The company's share structure, including any multi-class shares, should be disclosed to shareholders along with a description of any safeguards established to afford protection to minority shareholders against misuse or misappropriation of investee capital due to conduct by the company's board, its management or controlling shareholder.

- Sunset clauses should be included in company charters (for example limited to five years as a maximum) specifying that any multi-class share mechanisms will automatically lapse after a certain period or events at which point the enhanced voting shares will convert into shares to meet the "one share-one vote" requirement.

- There should be an adequate number of independent directors serving on the board and committees to act as a check on any controlling owner influence and to help ensure minority shareholder rights are upheld.

More generally, we are concerned that the EU's intentional language to restrict Member States from excluding multi-vote share structures in newly formed companies, as this will create an environment that will force Member States to adopt multi-vote share structures just to remain competitive in the IPO listing race. It will limit an EU Member State' ability to pursue its own unique effort to encourage SMEs to remain or list in their market by forcing them to adopt this language.

This intended Directive would also restrict investors from seeking out companies in which the capital they provide gives them the equal vote. For investors faced with the decision whether to invest in a company with multiple voting shares, the ICGN Global Stewardship Principles state:

> *"Protecting voting rights against dual class shares and other forms of differential ownership which have the practical effect of marginalising stewardship and the accountability of companies to minority shareholders by diluting their voting rights. This stands in sharp contrast to the ambition of stewardship to empower shareholders, through voting and engaging, to exercise their voice in direct proportion to their economic stake in a company.[7]"*

ICGN acknowledges that the EU will require all EU Member States to include a requirement for sunset provisions in the case of multi-class share structures. However, we caution that this could unintentionally encourage Member States who do not currently allow for multiple class share structures to ultimately adopt them. Furthermore, under the EU's proposed Article 5 regarding safeguards for fair and non-discriminatory treatment of shareholders of a company, we believe that the proposed safeguards are necessary but do not go far enough.

Article 5 has two requirements that must be implemented by Member States, including:

a. Ensuring that a company's decision to adopt a multiple-vote share structure and any subsequent decision to modify a multiple-vote share structure that affects voting rights are taken by the general shareholders' meeting of that company and are approved by a qualified majority as specified in national law. Where there are several classes of shares,

[7] ICGN Global Stewardship Principles 2020, p. 7.

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such decisions shall also be subject to a separate vote for each class of shareholders whose rights are affected.

ICGN recommends that the proposed language be expanded to explain in more detail how shareholders will be able to reach a "qualified majority", which should be more than 50%. ICGN Members have experienced their votes not being counted towards a majority in several cases. Broker votes, abstentions and non-votes by shareholders should be clarified to know if they count toward or against the qualified majority.

We also emphasise that the timing of the vote is critical. A company may make this decision in a general meeting made up of the founder and early investors which could be held before the IPO is issued. The language in the proposal for investors to have the opportunity to vote at a general shareholder meeting may therefore be too late for investors to support or modify a multiple-vote share structure.

b. Limiting the voting weight of multiple-vote shares on the exercise of other shareholders' rights, in particular during general meetings, by introducing either of the following: (i) a maximum weighted voting ratio and a requirement on the maximum percentage of the outstanding share capital that the total amount of multiple-vote shares can represent; (ii) a restriction on the exercise of the enhanced voting rights attached to multiple-vote shares for voting on matters to be decided at the general meeting of shareholders and that require the approval by a qualified majority.

ICGN recommends that the one-share, one-vote principle would provide a much clearer way for investors to vote effectively and have confidence that their voting power had not been diluted. If, however, investors are subject to multiple-vote structures, ICGN recommends that the EU adopt the following requirements:

- There should be a maximum duration of five years until the multi-class shares return to one-share, one-vote structures. Member States should harmonize this five-year limit to provide a uniform standard for all SME investments in the EU.

- Multi-voting rights should not be eligible to be transferred to third parties; i.e., if a founder or early investor receives multi-voting rights at the start, they should hold on to them for the duration.

- During the interim period, the maximum weighted voting rights ratio should be no more than 5:1.

- An adequate number of independent directors should be appointed to the board and committees to act as a check on controlling shareholder interests and protect the interests of minority investors.

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ICGN generally supports the proposal for a framework related to issuer-sponsored research in Article 24 (3b) and (3d) of MiFID II and the proposal to alleviate the research unbundling rules in

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Article 24 (9a) (c) of MiFID II. This may help increase the level of investment research on SMEs. We have more substantial comments on Article 1 and 33 as follows:

Article 1

Article 1 requires that "research provided by third parties to investment firms providing portfolio management or other investment or ancillary services and research prepared and distributed by such firms shall be fair, clear, and not misleading. Research shall be clearly identifiable as such or in similar terms, provided that all conditions applicable to the research are met".[8] The amendments also include a requirement that the research be labelled as "issuer-sponsored research" if is produced in compliance with a code of conduct developed or endorsed by a market operator registered in a Member State or by a competent authority, which sets out minimum standards of independency and objectivity to be complied with by the providers of such research. The Amendment also requires that a market operator (or the competent authority) will be required to publish the code of conduct on its website and review and re-endorse it every 2 years.

As the EU noted in the proposal, research on SME companies can be more challenging to obtain by possible investors and "the current low level of investment research on such issuers, driven by many underpinning factors, leads to their low visibility and scarce investors' interest, further limiting the liquidity for the already listed companies".[9] Investors must have the necessary research to conduct their own due diligence review prior to making any investment, especially with SMEs. The opportunity for growth and long-term value creation are strong incentives for investors to increase their portfolio allocation to SMEs. Gaps in reporting or thin research may give investors pause.

ICGN agrees that research which is prepared and distributed on behalf of an SME should be appropriately labelled. Information written and provided by issuers (or on behalf of an issuer), such as proxy voting materials and annual reports, should be clearly identified as having been developed by the issuer.

We note that research, if not appropriately labelled, may infer an independent review has been conducted by a qualified research entity. Therefore, any ties to an issuer should be clearly and prominently disclosed on the front page and within the research document as necessary.

Article 33

In Article 33, the Amendments give the Commission the power to adopt "delegated acts in accordance with Article 89 to supplement this Directive by further specifying the requirements laid down in paragraphs 3 and 3a of this Article. Those requirements shall take into account the need to maintain high levels of investor protection to promote investor confidence in those markets while minimising the administrative burdens for issuers on the market".[10]

ICGN understands that the EU is attempting to balance the costs of bringing a SME company into the public market with the need to ensure appropriate investor protections. This is reference as follows in ICGN's letter dated 22nd February 2022:

[8] EU Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL, p. 21.
[9] EU Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL, p. 2.
[10] EU Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL, p. 23.

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"Greater access by SMEs should assist investors with the opportunity to invest in companies and develop access to robust capital markets. However, providing SMEs with opportunities to make listing on EU public markets more attractive for companies should not come at the expense of investors, and we have concerns that some of the elements being considered by the EC in this initiative may have the effect of watering down important shareholder rights and protections.[11]"

Article 33, as amended, gives a grant of power that is unspecified other than the requirements within the Article. ICGN does not see a need to choose between high levels of investor protection versus minimizing the administrative burdens of bringing issuers onto the market. Both needs must be met; investors provide the capital that SMEs need to enter the market and as such, the Commission should maintain high levels of investor protection, while helping SMEs with any administrative burdens.

Finally, ICGN agrees that there is a need to harmonise and consolidate the Listing Rules by repealing the Listing Directive and transferring the relevant provisions into MiFID II under Article 51, as provided. ICGN has encouraged regulators to harmonise standards, where possible, to support investors and companies within the global capital markets.

ICGN is grateful for the opportunity to comment on this final consultation from the European Commission. We thank you for considering our perspective and remain at your disposal should you wish to discuss these matters further. If you would like to follow up with questions or comments, please contact me, or my colleague Carol Nolan Drake, ICGN's Governance & Stewardship Policy Manager (carol.nolandrake@icgn.org).

Yours faithfully,

Kerrie Waring
Chief Executive Officer, ICGN

CC: Catherine McCall, Chair, ICGN Global Stewardship Committee

[11] Consultation document - Targeted consultation on the listing act: making public capital markets more attractive for EU companies and facilitating access to capital for SMEs (icgn.org), p.1.

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