ICGN
International Corporate Governance Network
inspiring good governance & stewardship

Harriett Baldwin MP
Chair of the Treasury Sub-Committee on Financial Services Regulations
House of Commons
London SW1A 0AA

28 March 2024

Dear Rt Hon Harriett Baldwin,

Subject: FCA's Listing Reform Consultation

The International Corporate Governance Network (ICGN) welcomes the opportunity to respond to your letter dated 14 March 2024, regarding the Financial Conduct Authority (FCA)'s consultation CP23/31. You asked for our views on the proposals for listing rules reforms, "including whether they go far enough, whether they remove to many shareholder protections, and whether we think the timescale for the reforms to be implemented is sufficiently fast".

Led by investors responsible for assets under management of US$77 trillion, ICGN is an authority on global standards of corporate governance and investor stewardship. Headquartered in London, our membership is based in more than 40 countries - largely in Europe and North America, with growing representation in Asia. The ICGN Global Governance Principles and Global Stewardship Principles, written from an investor perspective, are widely used by our members in their company assessments and voting decisions, and by regulators when developing corporate governance rules.

ICGN believes that the FCA's proposals for listing rules reform will increase costs for investors and expose them to further undue risk. We would like to emphasize to the Treasury Committee that this may have significant negative implications for underlying beneficiaries including pensioners and retail investors' savings. In our view, the FCA does not explicitly reflect this in its cost-benefit analysis. Furthermore, at a time when the FCA is encouraging investors to play a greater, and more responsible, stewardship role in promoting the long-term success of companies through monitoring, voting and engagement, the imposition of weaker voting rights will have the opposite effect by inhibiting investor influence.

In the consultation document CP23/31,[1] the FCA highlights its ambition to introduce "the most far-reaching reforms of the UK's listing regime in three decades". The FCA notes that investors have expressed strong concerns over the proposed reforms. Despite investors' concerns, the FCA maintains its proposals, and goes further by removing a key investor protection mechanism: the mandatory time-based sunset clause for dual-class shares.

ICGN encourages the FCA to take investors' feedback into account. Investors recognise the challenges that the UK and other markets face with a reduced number of IPOs over recent years. However, they have expressed the view that, while it is unclear whether the changes proposed to the listing rule would help attract listing in the UK, the proposed reforms are likely to harm the UK's reputation as a market with robust investor protection, high corporate

[1] CP23/31: Primary Markets Effectiveness Review: Feedback to CP23/10 and detailed proposals for listing rules reforms

governance standards and a stable policy environment, thereby potentially reducing the attractiveness of UK listed companies.[2]

Factors such as liquidity, access to sophisticated investors with a deep understanding of the company's sector, valuation and research coverage, and the presence of comparable companies in the market are among the key factors that determine where a company chooses to list.[3] The speed of the process leading to the IPO, access to talent, and tax matters can also be key considerations. The FCA does not address these factors. We do not see any convincing evidence demonstrating that allowing dual-class shares structures or removing shareholder votes on transactions is an effective mechanism to attract listings

ICGN recommends that the FCA reconsiders its proposals. While we support the ambition to simplify the rules and reduce compliance burden for companies, we ask that the FCA maintains key shareholder protection mechanisms.

- **Dual class shares structures**

ICGN does not support the FCA's proposal on dual-class shares. Our preference would be that the FCA maintains the approach it introduced in 2021.

If the FCA decides to move forward with its proposed reform, we consider it essential that sunset clauses should specify that any multiple class share mechanisms will automatically lapse after a certain period or events, supported by a vote of independent shareholders after 5 to 7 years, and followed by an annual rolling vote. Empirical research shows that any benefits of dual-class share structures seems to dissipate after five to ten years. The research indicates that over time, and on average, the valuation of these firms tends to decline. See for instance the paper from Harvard Law School researchers Lucian A. Bebchuk and Kobi Kastiel,[4] the studies from the European Corporate Governance Institute,[5] the CII Research and Education Fund (August 2023),[6] former US SEC Commissioner Jackson,[7] and Investor Coalition for Equal Votes (ICEV)'s research (2023).[8]

We support the FCA's proposal to restrict the transfer of such shares, and that no further weighted voting rights shares should be able to be issued after listing.

Unequal voting rights are problematic because they dilute the voice of minority shareholders. They may serve to entrench management and allow founders and controlling shareholders to monopolise the decision-making, potentially putting minority shareholder interests at risk. In extremis such structures create opportunities for expropriation, with controlling shareholder gaining private benefits of control at the expense of minority shareholders.[9] Furthermore, the imposition of unequal voting rights has the effect of watering down investor influence.

[2] ICGN Statement on High Standards of Corporate Governance and Investor Protections as Pre-requisites for UK Capital Market Competitiveness and Growth, signed by more than 50 asset owners and asset managers, as well as investor associations globally, 9 February 2024
[3] UK Finance and EY, UK Capital Markets Building on Strong Foundations.pdf, May 2023
[4] Lucian A. Bebchuk and Kobi Kastiel, "The Untenable Case for Perpetual Dual-Class Stock," 103 Va. L. Rev. 585- 631 (June 2017), available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2954630
[5] Martijn Cremers, Beni Lauterbach and Anete Pajuste, "The Life Cycle of Dual-Class Firms," (November 2017) at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3062895
[6] James Crowe, "Dual-class structures and classified boards: Evidence from 2018-2023" (August 2023), CII Research and Education Fund,
[7] Commissioner Robert R. Jackson, Perpetual dual-class stock case against corporate royalty, 15 February 2024
[8] Investor Coalition for Equal Votes, Undermining the shareholder voice, 2023
[9] See ICGN Viewpoint on differential share ownership, 2017

Principle 9 of the ICGN Global Governance Principles emphasises the importance of equal voting rights for all shareholders, according to the ‘one share, one vote’ standard, a key aspect of shareholder democracy. We believe shareholders’ influence on the company’s decision-making should be proportionate to their economic exposure. In the event of the existence of multiple class shares, we insist that strong safeguards must be in place.

- **Shareholder vote on significant and related party transactions**

We also strongly encourage the FCA to maintain a mandatory shareholder vote for related party transactions and significant transactions above a certain threshold. The existing rules were introduced to provide the necessary checks and balances to protect the interests of minority shareholders from potential abuse. We are concerned that investors will be unable to block transactions that erode shareholder value. We note that, according to the OECD Corporate Governance Factbook 2023, a majority of jurisdictions surveyed require shareholder approval for related party transactions.

For more information, please find attached our full response to the FCA’s consultation CP23/31.

Finally, regarding your question on whether the timescale for the reforms is sufficiently fast, we believe the substance of the changes to be implemented is more important than the timescale itself. First and foremost, we need to make sure that the reforms will help address the issues identified by the FCA and do not have unintended consequences, including for people’s savings.

Thank you for the opportunity to share our perspective. ICGN members would welcome a discussion with the sub-committee, perhaps with a private hearing dedicated to this important topic. We remain at your disposal should you have any questions or comments. In this regard, please contact our Global Policy Director, Séverine Neervoort (severine.neervoort@icgn.org).

Yours faithfully,

Kerrie Waring
Chief Executive Officer, ICGN