Financial Conduct Authority
12 Endeavour Square
London
E20 1JN

By email: cp21-21@fca.org.uk

14 September 2021

Dear Sir, Madam

Re: Consultation Paper (CP21/21): Primary markets effectiveness review

We are writing on behalf of the British Private Equity and Venture Capital Association ("BVCA"), which is the industry body and public policy advocate for the private equity and venture capital industry in the UK. With a membership of over 700 firms, we represent the vast majority of all UK based private equity and venture capital firms, as well as their professional advisers and investors. Between 2016 and 2020, BVCA members invested over £47bn into around 3,500 UK businesses, in sectors across the UK economy ranging from heavy infrastructure to emerging technology. Companies backed by private equity and venture capital currently employ 1.1m people in the UK and 90% of the businesses our members invest in are small and medium-sized businesses.

Overview of BVCA recommendations

The BVCA supports, in principle, many of the measures proposed in this consultation, with many appearing to be well reasoned and balanced. We also applaud efforts by the FCA and others to promote the UK as an attractive place to do business. We consider that, if calibrated correctly and accompanied with other recommendations from the Lord Hill Listing Review, the proposals could support the objective of open and accessible markets with high standards that are trusted and transparent. However, we urge the FCA to review certain aspects of the proposals, where further clarity is needed, and to consider carefully whether some of the changes proposed are required.

- **Models for UK listing regime -** It is our view that there are strong arguments in favour of retaining the current two-segment structure, which gives investors the ability to choose whether they wish to invest in companies complying with the premium listing requirements, or those with lower corporate governance burdens. As such, Model 3 or Model 4 would be our preference if reforms were to be taken forward.

- **Indices -** It is important to note, that for issuers, a key benefit currently of seeking a premium listing, other than the perceived governance benefits by investors, is the eligibility for inclusion in an index.

- **Sponsors -** In the case of premium listings, financial and legal advisers are heavily involved in the preparation of the Company as a public issuer and preparing a disclosure and there does not seem to be any tangible benefit in having a sponsor in addition to those advisers.

- **Dual Class Share Structures -** We agree with the rationale for introducing DCSS to the premium listing segment and welcome the proposal, subject to certain changes as discussed in our response below.

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- **Free float requirements** - Free float is an important concern for issuers and given the lack of correlation between free float at IPO and subsequent liquidity, and the fact that free floats tend to increase over time, we support the proposed change.

BVCA responses to the consultation questions

We have limited our responses to those questions we believe are particularly relevant to our members.

Q1: Would a single segment for equity shares in commercial companies meet the needs of both issuers and investors?

In our view, the premium segment currently serves a useful purpose, providing assurance to investors that an issuer listed on the premium segment complies with the highest governance standards. Requirements related to related party transactions and significant transactions are seen as having value, and Model 1 mentioned in the consultation paper does not necessarily seem the right approach to reforming the current system.

Further, the premium segment requirements and the associated costs are not always appropriate or proportionate, in particular for smaller or emerging markets issuers. This means that Model 2 and the enhanced requirements for standard segment issuers may deter certain companies from listing in London. In the US, the corporate governance requirements do not depend on segment of the listing venue, the US rules differentiate between US and “foreign private issuer” and in certain cases, the latter can satisfy certain requirements if it follows home country rules.

In our view, there are strong arguments in favour of retaining the current two segment structure, which gives investors the ability to choose whether they wish to invest in companies complying with the premium listing requirements, or those with lower corporate governance burdens. Allowing the market to set the minimum standards, with FCA oversight to ensure an appropriate level of protection for retail investors (Model 4), may help the UK to compete with other jurisdictions as a listing venue, and promote innovation and flexibility; however, it could also lead to uncertainty over investor protections and undermine the LSE’s reputation for high standards of corporate governance. Model 3 may be a better model because it would enable the FCA to ensure the overall quality of issuers is maintained. For issuers, a key benefit currently of seeking a premium listing, other than the perceived governance benefits by investors, is the eligibility for inclusion in an index.

Notwithstanding the foregoing, we note that Nasdaq has three distinct market segments, the Nasdaq Global Select market, which is has most stringent listing requirements of the segments, the Nasdaq Global Market, and the Nasdaq Capital Market, which has the least stringent listing requirements of the segments. To list in a particular segment, a company must meet both the financial criteria, which depend on whether the Company is seeking to qualify for the respective segment based on, for instance, pre-tax earnings, cash flow, market capitalization or revenue, and the liquidity criteria, which depend on whether the Company intends to, for instance, launch an initial public offering, is currently trading common stock or is controlled by a company already listed on the Nasdaq Global Select Market. However, the corporate governance requirements are the same across all Nasdaq market segments, with limited exemptions for limited partnerships, foreign private issuers, initial public companies or companies controlled by a company already listed on the Nasdaq Global Select Market. We believe adopting a similar framework would permit the LSE to provide greater flexibility for issuers depending on their size and stage of growth.

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As mentioned in the consultation paper, the reaction of the indices to the alternative segment will be key to its success. It will be important that indices do not automatically exclude issuers listed on the alternative segment from index inclusion.

Q2: Which elements of the existing listing regime would you consider it most difficult or least desirable for issuers and/or investors to operate without? Are there any particular elements you would reinstate? i.e. the controlling shareholder regime, or the free float requirements.

Q3: Would the role of the sponsor be a significant loss? Is their role under any specific element of existing requirements considered significantly beneficial to issuers or investors currently?

For a standard listing, the financial and legal advisers of the company prepare it for a listing and its continuing obligations. In our view, in the case of premium listings, financial and legal advisers are heavily involved in the preparation of the Company as a public issuer and preparing a disclosure and there does not seem to be any tangible benefit in having a sponsor in addition to those advisers. We would welcome the removal of the requirement for a sponsor for the purposes of simplifying the listing process and reducing the issuer's ongoing compliance costs post-IPO. In addition, for reputational reasons, financial and legal advisers will continue to consider carefully which prospective listings or corporate transactions they wish to be associated with even if the requirement of a sponsor is removed, thereby preserving the quality of issuers listing in the UK. We also note that neither Nasdaq nor the NYSE require issuers to have a sponsor to be eligible to list, which has not impaired the reputation of US markets or those issuers who have listed on either exchange.

Q4: What would be the benefit of being admitted to the Official List rather than just admission to a trading venue?

By way of comparison, we note that in the US there is no equivalent to the Official List; instead, issuers are admitted to a trading venue where, in addition to US federal securities law requirements, the issuer also has to comply with the applicable requirements of the relevant exchange. We do not consider there to be any tangible benefit to requiring issuers to be admitted to the Official List in addition to being admitted to the trading venue in question.

Q5: Should we have a role in approving the admission criteria set by trading venues and/or indices? Could adequate investor protection be maintained if different trading venues compete on admission requirements?

We believe that adequate investor protection could be maintained if different trading venues compete on admission requirements. By way of example, in the US, the US federal securities law framework imposes a certain level of corporate governance requirements on issuers which allows the listing venues to set a standardised set of minimum corporate governance requirements while also setting their own admission criteria.

Q6: What types of issuers would find it hard to comply with the standards within the existing premium listing segment and why?

The current barrier to a premium listing for companies with a dual-class share structure prevents a large number of technology companies, private equity and venture capital backed companies and other founder-led growth companies from seeking a LSE listing, given that their owners/founders may want to retain some level of control of the company after its IPO through the use of a dual-class share

structure. The proposed DCSS changes should, however, address this. See below for our further comments on the DCSS proposal.

Q7: Do unlisted markets provide a suitable alternative to listed markets? Would a gap emerge for any particular type of issuer? Do you consider there would be any particular benefits or drawbacks to this approach?

We believe a strong OTC market (unlisted) would provide issuers with a good opportunity to test the interest for their securities before committing to a listing and incurring the associated costs. An example of where this is already in practice is the US OTC market for Level I ADSs.

Q8: What types of companies or strategies should the 'alternative' segment be aimed at?

We have no particular comments on this.

Q9: Do the existing provisions in the standard segment need to be changed to suit these companies, either through relaxation or to provide additional shareholder protections?

We have no particular comments on this.**Q10: How important is our role in setting additional admission standards to listing in the 'alternative' segment? Are there any benefits to this role being performed by us rather than a trading venue, or market discipline?**

See our response to question 5. We believe admission standards could be set by the exchanges, with the FCA focusing instead on implementing a standardised minimum threshold of corporate governance that would apply across all segments (subject to certain limited exceptions for certain types of issuers, such as non-UK companies).

Q11: Do you consider the alignment between admission to the index and admission to the 'senior' segment to be important? Should the indices consider setting more objective admission criteria?

Q12: How can the process for listing debt and debt-like securities be improved for issuers without jeopardising investor protection?

Q13: Should there be a separate listing segment for debt and debt-like securities?

Q14: Which particular elements of the listing regime could be tailored to improve their effectiveness for other types of securities? In what way?

We have no particular comments on these questions.

Q15: Do issuers consider the process of admitting further issues to both the FCA and the trading venue to be burdensome?

We note that, whilst the process can be duplicative and removing it would prove sensible, we do not believe that it is particularly burdensome for issuers.

Q16: Would the existing procedures conducted by trading venues to ensure issuers comply with their disclosure obligations (production of a prospectus) need to be enhanced if we were to cease admitting further issues to the Official List? What costs would be associated with these, if any?

It is our view that any response to this question would require further information in respect of the proposed regime for secondary issuances and the circumstances under which it is envisaged that a prospectus would be required. In any event, we would expect the FCA to continue to have a monitoring role to the extent a prospectus is required, but if it is envisaged that an alternative document can be produced for a secondary issuance, we consider that this process could instead be subject to the rules of the trading venues, which would be monitored by the FCA, as outlined above.

Q17: Are there any legal, regulatory or tax requirements that are connected with further issues being admitted to the Official List, that could not be maintained by further issues being admitted to a trading venue?

Other than issues caused by excessively restrictive drafting in contract covenants or investment policies, we see no legal, regulatory or tax issues with the proposal to cease the practice of admitting further issues to the Official List.

Q18: Do you agree with our rationale for introducing DCSS to the premium listing segment? Is there any additional evidence that we should consider?

We agree with the rationale for introducing DCSS to the premium listing segment and welcome the proposal, subject to certain changes as discussed below. Given the recent influx of founder-led venture capital backed fast-growing companies, particularly in the technology and life sciences sectors, in global markets, it has become clear that the lack of dual-class share structures for a premium listing has resulted in the LSE becoming an unattractive listing option; the proposed DCSS changes should go some way to addressing that.

However, it is imperative for the LSE's attractiveness that its reputation for high standards of corporate governance is maintained. We are concerned that the proposal to permit a DCSS ratio of 20:1 provides founders with excessive control that could in practice result in the effective disenfranchisement of non-founder shareholders. We therefore suggest setting the maximum ratio at 10:1, in line with HKSE rules and also commonly seen in the US. In addition, we are concerned that the proposal to permit holders of specified weighting voting rights shares to participate on voting to approve documents requiring prior approval (including employee share schemes and long-term incentive plans and discounted option arrangements under LR 9.4, related party transactions under LR 11 and dealing in own securities and shares as outlined in LR 12) undermines important shareholder protections, and we suggest that holders of specified weighting voting rights shares continue to be precluded from voting on such matters.

In any event, given the potential changes to the listing structure referred to in our response to question 1 above, if indices do not automatically exclude alternative segment listed companies from index inclusion, it is far less important that issuers with a dual class share structure be eligible for admission to the premium segment.

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Q19: Do you foresee any limitations to our proposal if the weighted voting shares are unlisted?

As noted in our response to the questions above, if indices do not automatically exclude alternative segment listed companies from index inclusion, it is far less important that issuers with a dual class share structure be eligible for admission to the premium segment.

Q20: Do you consider that a five year sunset period for DCSS in the premium listing segment is the correct length to protect companies from unwanted takeovers? Please provide evidence for your answer.

We think that the proposed period is appropriate and provides adequate protection from unwanted takeovers.

Q21: Do you consider that the mechanism proposed will be effective in providing a deterrent to unwanted takeovers? Please give reasons for your answer and any possible alternatives.

Please see question 20 above.

Q22: Do you agree with the proposed controls around DCSS in the premium listing segment? Are there any additional controls that would make the regime more effective?

Yes, we agree with the proposed controls. Please see our response to question 19.

Q23: Do you agree with our proposal to raise the minimum market capitalisation for companies seeking to list under standard and premium listing to £50m? If not, please state your reasons and indicate what alternative threshold may be more appropriate along with any supporting evidence. We also welcome views on whether we should consider setting out conditions under which we might modify the proposed rule on the new threshold, and if so what criteria stakeholders think we could usefully consider.

When considered together with the free float requirements, we agree with the proposal of £50 million. We note, however, that although it does not currently affect a large number of companies, introducing a £50 million minimum market capitalisation requirement does reduce flexibility for an issuer to decide on the market most appropriate to it, instead pushing smaller issuers towards venues such as AIM. Given the success of AIM, however, we acknowledge that this may be seen as a benefit of the proposal.

Q24: Do you consider that the current level of market capitalisation for listed debt remains appropriate? Please give reasons for your answer.

We have no particular comments on this.

Q25: Do you agree with our proposal to reduce free float to 10% and to remove current guidance on modifications? Please give your reasons.

Free float is an important concern for issuers and given the lack of correlation between free float at IPO and subsequent liquidity, and the fact that free float tends to increase over time, we support the proposed change. Issuers are restricted in how they issue equity in an IPO currently, as although a number of institutional investors are willing to subscribe for more than 5% of the share capital, the

free float requirements mean that the allocation to such investors has to be reduced. The current requirements put the UK out of step with many other jurisdictions, and do provide a disincentive to list in the UK. As an additional point, the automatic assumption that a 5%-plus holding should not count towards free float due to being a strategic holding does not always reflect reality. With the increasing amount of funds available for investment, many such holdings are not necessarily strategic or long-term.

One further concern is that under the current proposals, issuers can satisfy the free float requirement with only having 2-3 public shareholders. In our view this undermines the purpose of the free float requirement, and we propose that issuers should also be required to have a minimum number of public shareholders (similar to the approach taken by Nasdaq and the NYSE) in addition to the 10% free float to be eligible for listing.

An important practical point in connection with the proposed change to free float requirements is the reaction of the indices – whether they adjust their eligibility requirements accordingly to reflect a lower free float, or maintain their current free float requirements.

Q26: Would you find information about issuers' free float level useful to inform investment decision-making?

No. it is our view that investors have substantial access to information that provides a good indication of the level of liquidity in a company's shares, for example, information included on the LSE website. The burden on an issuer of publishing regular information about its free float (determined in accordance with the Listing Rules) would be disproportionate to the benefit.

In the event that such a requirement were to be introduced, we anticipate that there would be operational challenges for issuers in determining which registered holders are members of the same group or acting in concert with each other.

Q27: Do you agree with our proposal to leave track record requirements as they are now, based on our assessment that this would only affect a small number of stakeholders? If you disagree, please provide further evidence or examples of the wider impact this has on prospective listing applicants and proposed amendments.

We do not agree that the existing requirements affect only a small number of issuers. In our view, the track record requirements have caused significant additional work in a large number of actual and abandoned premium listing segment IPOs in which our members have been involved and do not, in any event, result in helpful disclosure for investors. For many prospective issuers, determining whether the financial information that has already been published or will be published in the prospectus will satisfy the eligibility requirement is not straightforward, and the issuer and its advisers may need to discuss the issue with the FCA.

Q28: What types of companies struggle to meet the existing requirement in the premium segment for a 3 year revenue track record covering 75% of the business? What alternatives could be considered for these companies?

Companies owned by private equity funds that are pursuing a 'roll-up' strategy – i.e. a strategy of investing in one company in a sector and then acquiring others, typically over a period of months or a few years, to create a combined entity with more commercial weight, which is then sold or floated.

We would suggest that investors should be protected by the prospectus disclosures and, if necessary, the issuer and its advisers should discuss with the FCA whether the prospectus needs to include information that goes beyond that specifically listed in the PRR and relevant Annexes.

Q29: Do you foresee any unintended consequences of these changes intended to modernise the Listing Rules, Disclosure Guidance and Transparency Rules and the Prospectus Regulation Rules?

Please see Appendix 1 for our response.

The BVCA would of course be willing to discuss this submission with you further - please contact Ciaran Harris (charris@bvca.co.uk) at the BVCA.

Yours faithfully,

Amy Mahon

Chair, BVCA Legal & Accounting Committee

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<u>Appendix 1 (In line with the City of London Law Society and Law Society response)</u>

<u>Glossary changes</u>

Definition of "trading day" (Annex A to Appendix 4): instead of saying "*(in LR and DTR) any day of normal trading in a share on a regulated market or MTF in the United Kingdom for this share*", we suggest this definition should say "*(in LR and DTR) any day on which securities of the relevant type are capable of being traded on a regulated market or MTF in the United Kingdom*". The same amendment should be made to the definition of "trading day" in Appendix 1 to the Listing Rules (Annex B to Appendix 4).

(For comparison, we note that the Rules of the London Stock Exchange do not define "trading day", but they do define "business day" as "*any day on which the Exchange is open for dealing*".)

<u>Changes to Listing Rules</u>

Copies of documents in electronic form

LR 1.4.9A: It is proposed that new 1.4.9A R should say: "*A reference to a copy (or copies) of a document in the listing rules includes a copy (or copies) of a document produced or stored using electronic means*." To be consistent with the definition of "document" in Appendix 1 to the Listing Rules and section 417 FSMA (which provides that a "document" includes information recorded in any form), we suggest this definition should refer also to a document being "recorded" – i.e. "*A reference to a copy (or copies) of a document in the listing rules includes a copy (or copies) of a document produced, <u>recorded</u> or stored using electronic means*."

A similar amendment should be made to DTR 1A.2.2 and 1C.2.2.

Cancellation of listing following a takeover

For context, the general rule in LR 5.2.5 is that if a premium segment issuer wants to cancel the listing of its shares, it must send a circular, obtain 75% shareholder approval and make certain announcements. However, this is subject to various exceptions in LR 5.2.10 (takeover where offeror was interested in 50% or less of the voting rights of an issuer before announcing its firm intention to make an offer), LR 5.2.11A (takeover where offeror was interested in more than 50% of the voting rights of an issuer before announcing its firm intention to make an offer) and LR 5.2.12 (a takeover or restructuring of the issuer effected by a scheme of arrangement, and certain other circumstances).

It is proposed that amended LR 5.2.11R should say:

> "*Where LR 5.2.10R applies, the issuer must notify shareholders and, in the case of certificates representing shares, holders of certificates:*
> *(1) by stating:*
> *(a) that the offeror has reached the threshold described in LR 5.2.10R(2);*
> *(b) that the notice period has therefore commenced; and*
> *(c) the anticipated date of cancellation, or*"

We suggest that for this purpose it should be sufficient for the issuer to make an RIS announcement - particularly as shareholders will by then have received a copy of the offer document in which, almost invariably, the bidder will state that, if the offer becomes or is declared unconditional in all

respects, and provided it has acquired or agreed to acquire shares in the issuer representing at least 75% of the voting rights, it intends to apply for the listing to be cancelled with effect from a date falling no earlier than 20 business days after the offeror has acquired or agreed to acquire that 75%.

We therefore suggest the rule should say:

"Where LR 5.2.10R applies, the issuer must notify a RIS:

(1) that the offeror has reached the threshold described in LR 5.2.10R(2);

(2) that the notice period has therefore commenced; and

(3) of the anticipated date of cancellation, or"

However, if the FCA considers that the issuer should send an individual notification to each holder of shares or DRs it would be helpful if the rule could make clear how the FCA expects such notification to be given (for example, by means of an individual notice sent electronically or in hard copy).

The same point applies to LR 5.2.11C.

References to disclosure or publication of documents, uploading to the NSM and filing documents with the FCA

We suggest that the FCA takes the opportunity to clarify in the Listing Rules, PRR and DTR (or perhaps by means of a Technical Note) what is meant by "filing a document with the FCA", as this term has slightly different implications in different circumstances. For example:

- **Prospectuses**: The final approved version of a prospectus must be filed with the FCA. However, under PRR 3.2.6G, the FCA itself will upload the final approved version of the prospectus to the NSM, and the issuer need do nothing further.
- **Circulars**: Under LR 9.6.1R, the final version of a circular to shareholders (meaning, where FCA approval is required, the final approved version) must be filed with the FCA by (the issuer) uploading it to the NSM.
- **Reports on payments to governments:** Under DTR 4.3A.10, such a report must similarly be filed with the FCA by (the issuer) uploading it to the NSM.
- **Disclosure of rights attached to equity shares**: Under LR 9.2.6F R, the prospectus, articles of association or other document setting out the rights and restrictions attached to shares must similarly be forwarded to the FCA for publication by (the issuer) uploading the document to the NSM.
- **Major shareholding notifications**: Under DTR 5.9.1R, a person making a notification to an issuer must, if the notification relates to shares admitted to trading on a regulated market, at the same time file a copy of such notification with the FCA. In this case, filing requires the person making the notification to complete a form TR-1 and submit it to the FCA via the major shareholdings notification portal on the ESS.
- **Other regulated information**: Under DTR 6.2.2, all (other) regulated information must be filed with the FCA. However, under DTR 6.2.3, an issuer can file regulated information with the FCA simply by making a RIS announcement - there is no need to follow a separate process to submit the information to the FCA (for example, via the ESS or by uploading a copy of the announcement to the NSM). Regulated information means information that an issuer is required to disclose under the DTR (such as annual and half-yearly financial results, reports on payments to governments, major shareholding notifications and details of general meetings), articles 17 to 19 of the UK Market Abuse Regulation (such as

announcements of inside information and details of PDMR dealings) or the Listing Rules (such as announcements relating to share issues, changes of directors and transactions).

Such clarification would also help issuers understand which information can be incorporated in a circular or prospectus, as LR 13.1.3 and PRR 2.7.1 allow information to be incorporated if it is included in a document published by the company that has been "filed with the FCA".

It would also be helpful to ensure that the wording used in each of the rules referred to above – some of which the FCA is proposing to amend - is consistent as far as possible. There are similar rules in chapters 14, 17 and 21 of the Listing Rules.

Profit forecasts in Class 1 circulars

We have no comments on the proposed amendments. However, we suggest that LR 13.5.32(1) should be amended to say *"comply with the requirements for a profit forecast or profit estimate set out in item 11.2 of Annex 1 of the PR Regulation"*.