The Investor Relations Society
5th Floor, 30 Coleman Street
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Capital Markets Policy
Financial Conduct Authority
12 Endeavour Square
London
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14 September 2021

Dear Sir or Madam,

Response to CP21/21 'Primary Markets Effectiveness Review'

Thank you for giving us the opportunity to comment on the FCA consultation: 'Primary Markets Effectiveness Review' (PMER). This response represents the views of the UK's Investor Relations Society ('the IR Society').

The IR Society's mission is to promote best practice in investor relations; to support the professional development of its members; to represent their views to regulatory bodies, the investment community and Government; and to act as a forum for issuers and the investment community. The IR Society represents members working for public companies and consultancies to assist them in the development of effective two-way communication with the markets and to create a level playing field for all investors. It has approximately 800 members drawn both from the UK and overseas, including the majority of the FTSE 100 and much of the FTSE 250.

We have considered and set out below our thoughts on a number of the issues raised in the consultation paper. Our corporate members are typically existing public market entities, but they have an ongoing interest in the reputation and functioning of the UK market, whilst as the IR Society we have a desire to see a flow of attractive and successful new entrants to the quoted arena. That is the perspective from which we have addressed the consultation.

A summary of our key points is set out below, both at the overall level and by the main topics of consultation, focusing on those areas where we believe our views are of the greatest relevance.

<u>Overall</u>

- We are supportive of the thrust of the recommendations and proposals made in the PMER. The long-term health and robustness of the UK financial system is critical to the UK economy, both as an important component of activity, but also as an enabler of competitiveness and growth across all sectors. While many elements contribute to its success, the listing regime is one of the most important in attracting both UK and international companies to the UK market.

- While it is encouraging to note the increase in IPO activity during the first six months of 2021, both in the UK and other markets around the world, the longer-term trends in the UK market are well documented, including the modest share of recent IPOs captured by London and the low proportion of technology listings compared to some other international trading venues. The IR Society is therefore encouraged to see actions now being proposed to address the factors which may be contributing to both the long-term decline in UK IPO admissions and the preference on the part of some issuers for other venues.

- We agree that the measures that the PMER proposes, including permitting dual class share structures (DCSS) for premium listings under certain conditions and lowering minimum free float requirements, would make London as a listing venue more attractive to issuers by bringing its rules closer to those of other global markets.

- We also believe it is important that any changes to the current listing regime are designed with flexibility to accommodate the opportunities and challenges of the future. Whilst there has been rapid growth in recent years in founder-led tech and latterly in SPACs, the next decade and beyond may see other trends and the system will need to accommodate their needs.

- Nevertheless, the IR Society believes that for the proposals to be successful it is important that any update to the listing rules occurs without compromising the high quality governance standards for which the London market is renowned. A UK listing should be seen as a means for companies seeking to benefit from the attractive liquidity and access to capital offered by its public markets, but without bringing in negative governance practices that could create reputational damage for the UK market. Accordingly, we favour a regime that maintains a clear role for the FCA and close adherence to the UK Corporate Governance Code, which leads us towards favouring Model 3, namely maintaining two broad segments for UK listed companies (enhanced version of the status quo).

Our comments below first address your request for views on the current listing regime, then the principal measures proposed to tackle barriers to listing more immediately.

<u>Functioning of the listing regime</u>
In the introduction to your discussion in section 3.2, you state that issuers, investors and advisors have told you [the FCA] that they don't understand the purpose of listing, particularly as a separate concept to being admitted to a particular market. In section 3.4, you also state that you consider there is duplication between certain requirements on issuers seeking admission of their securities to the Official List and admission to a trading venue. We would support practical moves to streamline the listing and admission procedures. However, as we state in our discussion of the various potential market models below, we believe that a valuable degree of confidence is provided to investors, to the ultimate benefit of issuers, by the FCA's role in supervising admission to the Official List. This in turn is utilised by a number of parties in their own index construction.

Turning to the potential models set out in your review, we appreciate that the different potential models for the UK listing regime outlined in the PMER are not intended to be discrete options. As such, we believe consideration should be given to combining some of the attributes of the various models. Our broad preference is to introduce more flexible rules for issuers, but within the broad umbrella of a similar regime to the one which currently applies.

Our comments on the four models presented are given below.

<u>Model 1: Create a single segment for UK listed companies and set the minimum possible requirements for eligibility for listing, at the level of the current standard segment</u>

- This proposal in our view would represent a relatively radical overhaul of the UK listing regime by moving the responsibility for setting rules to the market and trading venues, and by potentially taking away many of the existing requirements, for example for a sponsor, a full track record and corporate governance protections. We understand that taking this route would have the advantage of offering greater accessibility to the market for some issuers and could improve London's ability to compete for internationally mobile mandates.
- However, we believe reducing to a single segment that could accommodate all needs might be difficult to achieve. Additionally, this model arguably might put too much responsibility on the role of the trading venues and other parties through distancing the regulator from its oversight of key listing rules. There would be a risk that institutional investors could have less confidence without that comfort, whilst also a looser regime could be perceived as potentially increasing risks for retail investors.
- Our view is that this is a bigger step than necessary at this stage and we instead favour enhancing the existing model.

<u>Model 2: Create a single segment for UK listed companies and raise both eligibility and continuing obligations for all UK listed companies to that in the premium segment</u>

- While this model would likely result in a clearer distinction between listed and unlisted companies, we are not clear how this would achieve the objective of removing barriers to listing. In our view, there is a risk that this model would create a two-tier structure, with high requirements for entry to the group of premium companies, but pushing companies outside that bracket to seek alternative listing venues (including overseas) or indeed continue with private funding. This would be contrary to the general aim of encouraging new UK listings.
- While we can see the logic in considering removing the standard segment, not least the fact that it is not used by many companies and generally is seen as a category for those that cannot meet premium criteria, overall Model 2 seems to raise the bar too high.

<u>Model 3: Maintain two broad segments for UK listed companies (enhanced version of the status quo)</u>

- While recognising that none of the models is intended as a discrete option, the IR Society considers Model 3 to be the best of the four models presented. This is particularly in terms of maintaining clear and distinct visibility of the two segments for investors, keeping the key oversight linkages with the FCA, but also offering the flexibility to reduce barriers to listing, for example through introduction of DCSS and free float changes.
- We acknowledge however, that since this model is only an enhancement of the status quo, aligning to it may mean missing the chance to reconfigure significantly the UK listings regime, but in conjunction with some removal of current restrictions this could be an attractive option.

- Under Model 3, it will be important to take the opportunity to promote the 'alternative' segment as a home for high growth, entrepreneurial businesses, perhaps targeting those companies for whom the additional flexibility envisaged for the premium segment is still too onerous at this stage.

Model 4: Maintain two segments for UK listed companies but allow the market to set minimum standards for the 'alternative' segment

- This hybrid policy appears to be a mix of Models 1 and 3. In our view, the proposition for the market to set minimum standards for the alternative segment leaves the out-turn open to wide interpretation by different trading venues. On one level this would introduce scope for competition and variety from different offerings, but it could also create uncertainty and confusion for both issuers and investors.
- In general, this model appears to have similar benefits to Model 3. However, we consider the greater FCA role in Model 3 is valuable for investors, especially retail ones. We believe the FCA's role would be unnecessarily diminished if Model 4 is pursued.
- We are not convinced that the market will be as effective in "setting standards" and we believe there is tangible benefit from the FCA continuing to take that role.

Principal measures being targeted to remove deterrents to those seeking a UK listing

Turning to the more immediate measures proposed in the PMER, the IR Society is generally supportive of the measures that the FCA is consulting on. These should assist to overcome, or alleviate, some of the specific aspects of the Listing Rules which have been found to act as barriers to entry for certain issuers considering entry to the UK markets, thereby encouraging a wider group of companies to consider that option. Collectively, we believe the specific measures outlined in the consultation paper to improve access to a premium listing will likely prove beneficial. We have some reservations about the UK Listing Review's proposal that current exemptions should be broadened to include high growth innovative companies from other sectors, but note that the FCA is not proposing that extension at present.

We understand that primary markets regulation in general involves reaching a balance between the interests of issuers and investors. The introduction of securities of companies with dual class structures into the premium listing segment represents a departure from the traditional principle of "one share, one vote" and presents some risk to investors, since controlling shareholders will likely have a dominant influence over the governance during the life of the DCSS in certain important areas, including with respect to takeover approaches and removal of directors. Equally, we understand that the proposed change to free float requirements impacts liquidity, which is of importance to both investors and issuers.

However, for the reasons we set out below, we believe that these changes overall will potentially help in attracting a number of vibrant, growth-orientated companies to list on the UK market, which in turn will be of net benefit to investors too.

Targeted form of dual class share structures (DCSS) within premium listing

- The IR Society supports the introduction of a targeted and restricted form of DCSS within the premium listing segment in the belief that this would improve the attraction of a UK listing to a number of internationally mobile growth companies, frequently founder-led, when they are considering their options for a listing venue. Bringing such companies onto the market would potentially improve its diversity and growth profile. An active investor would continue to have the option whether to invest or not, if they had reservations about the reduction in short term influence consequent upon such a two-tier voting structure.

- There is a potential issue for passive investors, who would have to own these companies assuming they were included in the relevant indices, notwithstanding possible reservations about governance structure. However, there would be a potential offsetting positive if the change created a more dynamic growth mix in the indices.
- The requirement for these shares that carry weighted voting rights to be held by a director or a beneficiary of their estate for a time-limited period should also help assuage some concerns about the enduring influence of entrenched founders.
- We concur with the FCA's contention that the premium listing segment will continue to provide a degree of safeguard for shareholders, even if using the proposed specified form of DCSS, maintaining high corporate governance standards and investor confidence, for example through compliance with the broad principles of the UK Corporate Governance Code.
- We note that DCSS are commonplace in other markets, so their introduction into the UK premium listing segment should not stand out. In our view, DCSS will provide a time-limited opportunity for founders of high growth businesses to prove themselves in public markets and allow them to take a longer-term view on the early stage development of their businesses, without being under premature threat of losing control. Consideration could also be given to signalling to investors, notably for the benefit of the retail group, where a company employs a DCSS.

<u>Increasing the minimum market capitalisation threshold for new premium and standard listings from £700k to £50m</u>

- Though this represents a material uplift, the IR Society supports the proposal to increase the minimum market capitalisation threshold for new premium and standard listings from £700k to £50m.
- We believe that the proposed increase in the minimum market capitalisation threshold will benefit the main market, whilst also clearly differentiating the micro-cap company universe. For companies having an initial market capitalisation of less than £50m, AIM or other alternative market options should offer a viable initial entry point, with the option of moving to the main market later.

<u>Reducing the required free float level from 25% to 10%</u>

- We support a reduction in the required free float level from 25% to 10%, particularly in combination with an increase in minimum market capitalisation to preserve acceptable liquidity levels.
- We believe that the benefit in terms of attracting new listings from companies, including those with founder investors reluctant to sell too much equity too early, outweighs the potential downside of reduced liquidity. In the case of the smaller end of the market, the proposed increase in minimum market capitalisation for admission to the Official List should also help liquidity. Active investors will weigh up the merits of limited free float in the context of the wider investment case when contemplating an investment. Additionally, limited free float companies would form only a small part of any index weighting for tracking/benchmarking purposes, so "forced" exposure would be proportionate.
- In any event, many IPOs involve the sale of at least 25% of the equity, as issuers seek to raise additional capital to grow and, or, at the same time investors look to realise some

of their earlier investment. In these situations, lowering the threshold to 10% is not relevant anyway.

<u>Showing more willingness to allow waivers for the coverage of the 3-year track record of historical financial information</u>

- We understand the potential attraction of easing the current requirement to show a 3-year track record in respect of at least 75% of the revenue of a potential new issuer and the related provisions for specialist companies to provide alternatives to the standard information. In the case of high growth, innovative companies, this could further ease the burden of listing and encourage them to come to the quoted market earlier than they would otherwise, while at the same time providing investors with an opportunity to participate at a similarly early stage. In some of the companies where recent growth has been rapid this could be a particularly helpful dispensation for the issuer.
- However, this may reduce the available information on which investors would base their decisions and we note your [FCA] observation that the number of companies that would benefit from the dispensation would likely be small, given the separate prospectus requirements. Accordingly, we agree with your suggestion that at this stage there is no compelling reason to ease the existing Listing Rules.
- We do, however, agree that it is worthy of consideration whether there would be merit in extending the provisions currently granted to certain companies, in science based, minerals or property sectors, to a wider range of companies. It would be important for this to be clearly flagged, particularly to retail investors, given the higher risk that inevitably attaches to such earlier stage companies.

We hope you find these comments useful. Please do not hesitate to contact me if you have any further questions.

Yours sincerely,

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