Allowing dual class share structure companies in the Premium listing segment of the London Stock Exchange: appreciating international experiences and recognizing local conditions

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Key points

- In November 2020, the Chancellor of the United Kingdom (UK) announced a review of the UK's listing regime.
- One issue where public response is being sought is whether dual class share (DCS) structure companies should be allowed in the Premium listing segment of the London Stock Exchange (LSE).
- The New York Stock Exchange (NYSE) has long allowed companies with such a share structure to be listed. Both Singapore and Hong Kong amended their listing rules in 2018 to allow companies with such a share structure to list on their main board, subject to certain safeguards and restrictions.
- This article discusses why the UK should allow DCS structure companies in the Premium listing segment of the LSE from a commercial perspective and what measures the UK should adopt in allowing companies with such a share structure in the Premium listing segment. In doing so, it will also refer to other major financial markets in the world and examine how other jurisdictions have handled the issue of DCS structure companies.

1. Introduction

While 'one share, one vote' has been widely recognized as a bedrock principle of good corporate governance in protecting shareholders' basic rights,[1] some regulators consider this principle to be too inflexible to cater for investors with different risk appetites and issuers with different profiles. For example, entrepreneurs may wish to raise equity capital to finance some promising growth of their companies, but at the same time, they do not want to surrender too much control of their companies to those outsiders who may have different views on how to operate the companies. If all stock exchanges stick to the 'one share, one vote' principle, these entrepreneurs may prefer not to offer shares of their companies to the public and simply shelve those growth projects indefinitely until they can solicit sufficient funding from other sources. In this case, economies may suffer and investors may lose promising investment opportunities with handsome returns.

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1 Eg in the third OECD Principles of Corporate Governance, a good corporate governance framework should ensure equal treatment of all shareholders, including minority and foreign shareholders. All these shareholders should have the opportunity to obtain effective redress for the violation of their rights.

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One possible solution to this dilemma is to allocate differential voting rights so that one group of shareholders holding the same class of shares carries disproportionate voting rights.[2] These companies are said to possess a dual class share (DCS) structure.[3] By holding superior voting shares and selling the rest of the shares with inferior voting rights, entrepreneurs can obtain sufficient funding to finance the expansion of their companies and at the same time maintain their control. However, those holding superior voting shares will not receive shares of the residual gains or losses from new investments commensurate with their control; they may have incentives to make sub-optimal corporate decisions beneficial to themselves but harmful to the companies and those holding inferior voting shares.[4] The simple existence of this possibility of abuse from controllers of companies with a two-tier share structure may erode investors' confidence, deterring them from investing in these companies.

This article is therefore written against such a background and discusses the recent review of the UK's listing regime[5] announced by Rishi Sunak, the UK Chancellor, in considering whether DCS structure companies be permitted in the Premium listing segment of the London Stock Exchange (LSE).[6] The article is divided into the following sections. Section 2 will examine the arguments for and against DCS structure from a theoretical perspective. Section 3 will look at how other major financial markets with similar Global Financial Centres Index (GFCI)[7] score and rankings (namely: the USA, Singapore and Hong Kong) have handled the issue. Section 4 will look at the present treatment of DCS structure companies in the financial market of the UK and rationales of conducting a review of its listing regime. Section 5 will offer suggestions that with some appropriate governance measures put in place to ensure high standards of corporate governance are maintained, the UK should allow DCS structure companies in the Premium listing segment of the LSE. It is ultimately argued that as other major financial centres have allowed companies with such a structure to list primarily on their main board, there is no reason why the UK should not do so in order to strengthen the competitiveness of its financial market, providing there are appropriate measures in place to safeguard the interests of investors. Section 6 concludes.

2 Henry TC Hu, 'New Financial Products, the Modern Process of Financial Innovation, and the Puzzle of Shareholder Welfare' (1991) 69 Texas Law Review 1273, at 1294.

3 DC Ashton, 'Revisiting Dual Class Stock' (1994) 68(4) St. John's Law Review 863–960, at 866.

4 FH Easterbrook and DR Fischel, 'Voting in Corporate Law' (1983) 26 Journal of Law and Economics 395–427.

5 HM Treasury, 'Policy Paper—Call for Evidence—UK Listings Review' 19 November 2020, <https://www.gov.uk/government/publications/uk-listings-review/call-for-evidence-uk-listings-review> (accessed, 14 June 2021).

6 Question 2.1 of the UK Listings Review.

7 The GFCI is a ranking of the competitiveness of financial centres based on over 29,000 financial centre assessments. The first index was published in March 2007 and, since 2015, it has been jointly published twice per year by Z/Yen Group in London and the China Development Institute in Shenzhen. It is widely quoted as a source for ranking financial centres. New York, London, Hong Kong and Singapore have been consistently ranked as the world's top four financial centres by the index between 2007 and 2017.

2. Pros and cons of dual-class share structure

Traditionally, shareholder advocacy groups such as the Institutional Shareholder Services in the USA look unfavourably upon DCS. It is argued that an unbalanced system of voting rights is likely to hurt a company's corporate governance rating, which may in turn affect how institutional shareholders treat the company.[8] Such an argument hinges on the importance of shareholders' voting rights which is based on the theory of shareholder primacy. This essentially means that companies exist to serve the interests of shareholders, or more specifically, the theory mandates that the company be run with the goal of maximizing shareholder wealth.[9]

Shareholder primacy is simply viewed as a democratic legitimacy argument: the company must keep shareholder interests at the forefront because shareholders are the voting polity. Corporate law scholars such as Easterbrook and Fischel in the 1980s provided a justification for this theory.[10] In looking to ground shareholder primacy in economic theory, they looked to the traditional economic utility rationale of creating the highest level of efficiency or overall social utility.[11] This argument returns us to the 'nexus of contracts' models,[12] instead of being owners of the company. In these models, shareholders were one group of many whose contracts with one another jointly created the fictional corporate entity. Based on this analogy, it is argued that shareholders are the sole 'residual claimants' to the company's income. Creditors or bondholders have fixed claims, and employees generally negotiate compensation schemes in advance of performance. The gains and losses from any good or bad corporate performance are the lot of the shareholders, whose claims stand last in line.[13] As residual claimants, shareholders are therefore the group with the appropriate incentives to make discretionary decisions because right to vote (ie the right to exercise discretion) follows the residual claim.[14] Therefore, the existence of DCS whereby one class of shareholders enjoy inferior or no voting right for example, undermines the shareholder primacy theory.

Yet it is often argued that the shareholder primacy theory is based on the notion of 'shareholder homogeneity', which assumes that all shareholders are similarly situated and share similar interests.[15] However, in reality, shareholders may have very different economic interests depending on a variety of factors. One of the main assumptions behind the one share, one vote norm is that shareholders have a uniform interest in wealth

8 GM Hayden and MT Bodie, 'One Share, One Vote and the False Promise of Shareholder Homogeneity' (2008) 30(2) Cardozo Law Review 445–505, at 471.

9 DG Smith, 'The Shareholder Primacy Norm' (1998) 23 Journal of Corporation Law 277.

10 Above Easterbrook and Fischel (n 4).

11 FH Easterbrook and DR Fischel, *The Economic Structure of Corporate Law* (1991) Harvard University Press, 73.

12 MC Jensen and WH Meckling, 'Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure' (1976) 3 Journal of Financial Economics 305, at 310–11.

13 Hayden and Bodie (n 8), at 453.

14 Ibid, at 454.

15 Ibid, at 477.

maximization. Since all shareholders are entitled to part of the residual, they all have an interest in maximizing the size of that residual. But this assumption is not empirically correct.[16] Even if we assume that the ultimate goal of the majority of shareholders is to maximize wealth, different shareholders may have different time horizons for this maximization.[17] For example, some shareholders have yearly or quarterly profit margins to meet, some may have bought the shares looking to take it over, and then either buy all of the stock or walk away, and other shareholders buy the stock on a bet that the takeover attempt will succeed. In short, shareholders can have different notions of what wealth maximization means.[18] Moreover, many shares in large corporations today are widely held by groups from pension funds representing government employees to sovereign wealth funds controlled by overseas governments, who may have other interests that differ from those of the traditional private shareholders.[19] Therefore, the varying interests of shareholders do not comport with the notion of a shareholder electorate with one homogenized goal. Hence shareholders will not have the same preferences and they will not seek to effectuate those standards in lock-step voting patterns.[20]

Those who oppose DCS also assert that the use of such a share exacerbates collective action, free riding and passivity problems that lead to disenfranchisement.[21] This is based on empirical studies which demonstrate that the ownership composition of companies recapitalizing with DCS is often characterized by large family or management ownership groups[22] and below average institutional holders.[23] Due to their ownership arrangements, a large proportion of public shareholders would have to vote against any proposed governance measure for it to be defeated.[24] Furthermore, with lower than average institutional holdings, the outsider-shareholder group is thought to exhibit a high share turnover rate as well as to suffer the consequences of dispersed holdings.[25] Hence the costs of opposition are higher than normal because communication and coordination expenses rise in proportion to the extent of shareholder dispersal.

Several recent shareholder controversies have involved corporations with DCS. The Murdoch family owns about 12 per cent of News Corporation but controls almost 40 per cent of the votes, through a special class of shares which have superior voting rights.[26]

16 Ibid, at 492.

17 I Anabtawi, 'Some Skepticism about Increasing Shareholder Power' (2006) 53 UCLA Law Review 561, at 579–83.

18 Hayden and Bodie (n 8), at 493.

19 Ibid, at 487–91.

20 Ibid, at 502.

21 JN Gordon, 'Ties that Bond: Dual Class Common Stock and the Problem of Shareholder Choice' (1988) 76(3) California Law Review 40, at 44–45.

22 MM Partch, 'The Creation of a Class of Limited Voting Common Stock and Shareholder Wealth' (1987) 18 Journal of Financial Economics 313, at 332.

23 Ashton (n 3), at 908.

24 Gordon (n 21) at 46.

25 L Lowenstein, 'Shareholder Voting Rights: A Response to SEC Rule 19c-4 and to Professor Gilson' (1989) 89 Columbia Law Review 979.

26 'Dual-class share structures: The cost of control' *Economist* (21 July 2011). Since the News Corp. hacking scandal there have been calls from shareholders for a change in the share structure.

Such DCS structures are quite prevalent, especially in media companies and they can shield managers from stock market short-termism and hostile takeovers. But two studies conducted by Paul Gompers, Joy Ishii and Andrew Metrick, covering the years from 1994 to 2002, found that DCS companies perform worse than comparable companies where all shares confer equal voting rights.[27]

Technology companies also prefer DCS structures because they allow founders to raise capital without surrendering control. Google's IPO in 2004 involved two classes of shares. Before Facebook went public in 2012, it too created two classes of shares. Despite owning just 18 per cent of the company, Mark Zuckerberg, the founder, controls 57 per cent of the voting shares. Facebook's US$16 billion IPO in May 2012 generated huge investor interests but the shares subsequently slumped in price (though its share price has recovered significantly since 2013).[28] Critics have claimed that the controlling families and shareholders do not have proper incentives because they do not have the same economic risk as the other shareholders.[29] However, such criticisms can be rebutted on the basis that shareholders knew what they were getting when they purchased the shares. Corporate law should facilitate private ordering and choice, which includes the possibility that certain shareholders will accept less control as part of the bargain. This may mean a cheaper price and shareholders should be allowed to make this bargain if they wish to do so.[30] In fact, one study finds that DCS do not trade at a big discount on stock markets. Dual class IPOs achieved only slightly lower price-earnings and price–sales ratios than comparable single-class IPOs.[31]

The above arguments illustrate that the issuance of DCS may or may not be in the best interests of shareholders, but such an ownership model does not show any sign of going out of fashion.[32] It seems that whatever views one may hold about DCS structures, they are likely to stay and remain popular for certain sectors and companies. Therefore, it is important that we understand the development of the dual-class common share and its interplay with corporate control markets. The next section will therefore look at how major financial markets across the world have handled the issue of DCS structure.

27 P Gompers, J Ishii and A Metrick, 'Extreme Governance: An Analysis of Dual Class Firms in the United States' (2010) 3 Review of Financial Studies 23; P Gompers, J Ishii and A Metrick, 'Corporate Governance and Equity Prices' (2003) 118(1) Quarterly Journal of Economics 107–55.

28 'Facebook's IPO and Dual-Class Share Structures' *New Yorker* (28 May 2012). The value of Facebook's share has fallen from US$38 since its launch on 18 May 2012 to US$20 on 20 August 2012. Since 2013, its share price has recovered significantly and as of early 2021, it has been trading at more than US$266 on NASDAQ.

29 Hayden and Bodie (n 8), at 482.

30 Ibid, at 482.

31 S Smart and CJ Zutter, 'Dual Class IPOs are Underpriced Less Severely' (2008) 43(1) Financial Review 85–106.

32 Between January and June 2019, there were 15 dual-class IPOs in the USA, accounting for 26% of IPOs for the first half of that year (source: Council of Institutional Investors, <https://www.cii.org/files/2019%20Dual%20Class%20Update%20for%20Website%20FINAL(2).pdf>).

3. Dealing with dual share structure by major financial markets

United States

In the 1920s, public reaction instigated by academics and government officials in the USA became concerned with the growing power of the voting trusts and the investment banking community. In response, in January 1926, the New York Stock Exchange (NYSE) first disapproved the issuing of non-voting common shares.[33] In May 1940, the NYSE adopted a formal listing requirement relating to the use of DCS and the standard remained in effect without any incident for the next 40 years.[34] Subsequent attempts by listed companies to use DCS were rejected by the Exchange,[35] and no serious challenges to that policy occurred until the mid-1980s.

The DCS debate re-emerged as a result of an issuance of restricted shares by General Motors (GM) in conjunction with its acquisition of Ross Perot's Electronic Data Systems Corporation in 1984. The debate gained further momentum following the subsequent issuance of disparate voting shares by over 40 companies between the time of GM's issuance and June 1987.[36] The significance of the GM case was its explicit challenge to the NYSE policy that it represented. Moreover, an increasing number of family-controlled companies needed access to capital only available in the open exchange markets. DCS was therefore a means of gaining access without the control dilution normally associated with new equity issuances. Meanwhile, the NASDAQ (NASD) and the American Stock Exchange (AMEX), with less restrictive dual-class listing standards, were becoming increasingly competitive in the market for corporate listings.[37]

In light of the above concerns, the NYSE appointed the Subcommittee on Shareholder Participation and Qualitative Listing Standards in June 1984 to review its dual-class listing standards.[38] At the same time, the NYSE imposed a delisting moratorium for dual-class capitalizations and recapitalizations that contravened the NYSE policies on voting rights.[39] In January 1985, the subcommittee recommended a new listing standard by which listed companies would be permitted to issue common shares with unequal voting rights provided four conditions were met: (i) two-thirds of all shareholders entitled to vote would have to approve the creation of the second class of common share; (ii) if the issuer had a majority of independent directors at the time the matter was voted on, approval by a majority of these independent directors would be required. If the issuer did not have a majority of independent directors, the approval of all such directors would be required; (iii) the low-vote shares could not have a voting differential of more than 10 to 1; and (iv) the

33 J Seligman, 'Equal Protection in Shareholder Voting Rights: The One Common Share, One Vote Controversy' (1986) 54 George Washington Law Review 687, at 697.

34 *NYSE Listed Company Manual*, 1985, s 313 (A), (C).

35 NYSE delisted Cannon Mills in 1962 after the company distributed non-voting common shares to its common shareholders.

36 MG Warren III, 'One Share, One Vote: A Perception of Legitimacy' (1988) 89 Journal of Corporation Law 92–3.

37 Ashton (n 3), at 896.

38 Seligman (n 33), at 701–6.

39 RS Karmel, 'Qualitative Standards for Qualified Securities: SEC Regulation of Voting Rights' (1987) 36 Catholic University Law Review 809, at 817.

other rights attached to the restricted voting shares must be substantially the same as the rights of the high-vote shares.[40]

Many commentators at the time suggested that these recommendations were primarily based on the fierce competition from the NASD and the AMEX, as well as member dissatisfaction with the inflexibility of the existing rules as related to takeover defence. The NYSE subcommittee recommendations triggered an immediate congressional reaction that ultimately proved unsuccessful.[41] Following the dissemination of the subcommittee's recommendations, officials of the Securities and Exchange Commission (SEC), the NYSE, the NASD and the AMEX arranged for a series of meetings intending to resolve the lack of uniformity among the exchanges, yet their discussions proved unsuccessful. Shortly after the discussions concluded, the NYSE proposed a new, revised amendment to its Listed Company Manual which was even less restrictive than the original subcommittee's recommendations.[42]

The proposed standard for voting rights required delisting only if the recapitalization was not approved by a majority of independent directors and a majority of shareholders. Under this proposal, listed companies that created disparate voting rights shares during the NYSE moratorium would have 2 years from the date of the proposal's approval to comply with the amendment. Companies thereafter applying for listing would have to comply with the rule before listing could be approved. Furthermore, no exchange approval would be necessary if the disparate voting class was outstanding when the company first went public, or if disparate voting shares were distributed pro rata among a distributor's common shareholders in a spin-off transaction in which the distributor was not the issuer.[43]

In response to the second NYSE proposal and the failure of the three exchanges to reach a consensus on a minimum rule, the SEC eventually took action itself in June 1987 and created Rule 19c-4. This rule explicitly prohibited the exchanges from listing, or continuing to list, the securities of an issuer that takes action resulting in the nullification, restriction or disparate reduction of the per-share voting rights of holders of the company's outstanding common shares or resulting in the creation of a ceiling on the voting power of any one individual shareholder.[44] New issues were unaffected and could be listed without exceptional regulation of voting rights. The rule permitted companies to issue non-voting common share or a special class of common share with limited voting rights, as long as it did not dilute the voting power of existing shareholders.[45] The rule also enabled

40 NYSE, *Dual Class Capitalization: Initial Report of the Subcommittee on Shareholder Participation and Qualitative Listing Standards*, (NYSE: New York, NY, 1985) 3.

41 See *Hearings on the Impact of Takeovers on Shareholders, Before the Sub-comm. On Telecommunications, Consumer Protection, and Finance*, 99th Cong., 1st Sess., 1985. Some Senators expressed fear that anything less than one share, one vote rule would trigger a 'race to the bottom' among the exchanges.

42 Ashton (n 3), at 898.

43 Ibid, at 898.

44 In 1988, the SEC announced the adoption of Rule 19c-4 under the Securities Exchange Act 1934. The rule was adopted on 7 July 1988.

45 KD Bayley, 'Rule 19c-4: The Death Knell for Dual-Class Capitalizations' (1989) 15 Journal of Corporation Law 7.

a company to issue common shares with lower voting rights when engaging in a business merger or acquisition, as long as the company made the merger or acquisition for a bona-fide business purpose.[46] The SEC received 1100 comment letters and elicited testimony from 17 people on Rule19c-4. Amongst those comment letters, 1000 supported adopting the rule, of which 800 were submitted by individual members of the US Shareholders Association, which advocated a one share, one vote standard with no exceptions.

However, Rule 19c-4 generated much debate not just regarding the desirability of DCS, but on the larger issue of shareholder behaviour theory and the role of federal government in corporate governance and financial regulation. There was widespread criticism that the SEC's intervention into areas traditionally left to state regulation was improper. Thirty-two commentators who expressed opposition to the adoption of the rule during the SEC's consultation stage questioned its authority to adopt a rule in the area of qualitative listing standards. The opposition included the American Bar Association and the Business Roundtable.[47] The Business Roundtable eventually filed a suit in the Court of Appeals for the District of Columbia Circuit to vacate the rule on the basis of a theory grounded in corresponding notions of federalism. Rule 19c-4 was eventually struck down by the DC Circuit in June 1990 and DCS regulation was once again handed back to the exchanges and the states.[48]

Since the *Business Roundtable* decision, both the NYSE and the NASD have adopted enforced listing standards embodying the spirit of Rule 19c-4. In June 1992, the NYSE proposed a new listing requirement that would allow its listed companies to establish unequal voting rights. Unlike the NYSE, the AMEX had not adopted Rule 19c-4 before the decision by the court of appeals, and unlike the NASD, the AMEX had a pre-existing voting-rights policy.[49] Hence the immediate effect of the court decision for the AMEX was a reinstatement of the original policy before Rule 19c-4 was enacted. In September 1990, the AMEX appointed a Special Committee on Shareholder Voting Rights to recommend an appropriate listing standard. Adopted in April 1991, the proposed AMEX rule seeks to provide a balance between flexible capital structuring and managerial accountability.[50] It requires that companies seeking to recapitalize into a multiple-class structure or to issue additional shares of a higher-voting class must obtain favourable votes from two-thirds of their outstanding shares or a majority of shares unaffiliated with management or the controlling group. Moreover, the AMEX decided that a multiple-class company should have at least one-third of its board composed of independent directors or provide that holders of the lesser voting class be entitled to elect exclusively at least 25 per cent of the board.[51]

46 Ashton (n 3), at 899.

47 Above n 45 at 14.

48 *Business Roundtable v SEC*, 905 F.2d 406 (DC Cir 1990).

49 Proposed Rule Change By American Stock Exchange, File No SR-AMEX-91-13, 11 June 1991.

50 Ashton (n 3), at 902.

51 Above (n 49), at 27.

Likewise, in May 1994, the NYSE Board of Directors voted to modify the Exchange's voting rights policy, which had been based on Rule 19c-4. In the NYSE's own words, its policy is 'more flexible'[52] than Rule 19c-4, where it permits issuances by listed companies that would have been permitted under Rule 19c-4, as well as other actions or issuances that are not inconsistent with the new policy. Section 313(B) of the NYSE Listed Company Manual stipulates that the exchange's voting rights policy permits the listing of the voting common stock of a company which also has outstanding non-voting common stock as well as the listing of non-voting common stock. However, certain safeguards must be provided to holders of a listed non-voting common stock: (i) any class of non-voting common stock that is listed on the Exchange must meet all original listing standards. The rights of the holders of the non-voting common stock should, except for voting rights, be substantially the same as those of the holders of the company's voting common stock; and (ii) although the holders of shares of listed non-voting common stock are not entitled to vote generally on matters submitted for shareholder action, holders of any listed non-voting common stock must receive all communications, including proxy material, sent generally to the holders of the voting securities of the listed company.[53] The NYSE's interpretations under the policy will be flexible, recognizing that both the capital markets and the circumstances and needs of listed companies change over time.[54]

Today the regulation of voting rights is primarily governed by the rules of the exchanges and state law.[55] No state departs from a one share, one vote default rule, although state blue sky laws[56] often impose restrictions on the sale of some shares with disparate voting rights. Also, 18 states have adopted regulations prohibiting the issuance of common stock with unequal voting rights.[57] Hence state securities regulators represent an important supplement to exchange-based regulation. An interdependency exists between blue sky rules and the exchanges. State exemptions are the very foundation upon which the use of DCS vests.[58] Therefore, state exemptions granted to the NYSE and the AMEX listed companies are of great importance.

The SEC continues to assert that voting rights are fundamental and that a majority of current shareholders should never be permitted to diminish or eliminate the voting rights of an opposed minority. Yet since the *Business Roundtable* decision, SEC opposition is no longer of paramount importance.[59] Although it has been argued that the current case-by-

52 See NYSE Inc, *Listed Company Manual*, s 313 Voting Rights.

53 See s 313(B) of the NYSE Listed Company Manual for details.

54 See s 313(A) of the NYSE Listed Company Manual for details.

55 SM Bainbridge, 'The Short Life and Resurrection of SEC Rule 19c-4' (1991) 69 Washington University Law Quarterly 565, at 574.

56 A blue sky law is a state law in the USA that regulates the offering and sale of securities to protect the public from fraud. Specific provisions of these laws vary among states and they all require the registration of all securities offerings and sales, as well as of stockbrokers and brokerage firms. Each state's blue sky law is administered by its appropriate regulatory agency and most also provide private causes of action for private investors who have been injured by securities fraud.

57 Seligman (n 33), at 713.

58 Ashton (n 3), at 905.

59 Ibid, at 904.

case posturing of the NYSE has only exacerbated the uncertainty[60] and the debates surrounding dual-class common share remain a touchstone of corporate governance in the USA.

Having examined how the regulators in the USA have handled the issue of DCS structure, the article shall now turn its focus to the Asia-Pacific and explore the approach adopted by the regulators in Singapore and Hong Kong in handling DCS structure.

Singapore

In October 2007, Singapore's Ministry of Finance (MOF) set up a Steering Committee to carry out a fundamental review of its Companies Act aimed at ensuring an efficient and transparent corporate regulatory framework that supports the nation's growth as a global hub for businesses and investors.[61] The committee published its consultation paper in June 2011 and made a number of recommendations with regard to shareholders' rights.

Under section 64(1) of its prior Companies Act 2006, each equity share issued by a company must confer the right at a poll at any general meeting of the company to one vote in respect of each equity share unless it is a management share issued by a newspaper company under the Newspaper and Printing Presses Act.[62] The 2011 consultation paper proposed a change in the law allowing public companies to issue non-voting shares and shares carrying multiple votes.[63] According to the Steering Committee, most of the respondents during the consultation period agreed that public companies should be allowed to issue non-voting shares or shares with multiple votes, subject to certain safeguards.[64] The rationale behind this, according to the committee, is that it would allow companies greater flexibility in capital management. Furthermore, it would be up to the Singapore Exchange (SGX) to determine whether listed companies should be allowed to issue such shares.

However, during the consultation stage there was a minority of respondents who expressed concerns that the proposal risks undermining minority rights and compromising standards of corporate governance. They argued that Singapore is different from other western developed markets because Singaporean companies are predominantly controlled by a group of shareholders. Hence shares with multiple votes can be used to severely undermine minority interests.[65] Companies in Singapore generally grow out of a majority family-owned environment or government-controlled entity.[66] Until recently, government ownership was a key feature of the corporate landscape in Singapore. Up to 80 per cent of some government-linked corporations (GLCs) are directly and indirectly

60 Ibid, at 904.

61 Singapore MOF, 'Report of the Steering Committee for Review of the Companies Act', Consultation Paper, June 2011.

62 Companies Act 2006, s 64(1).

63 Singapore MOF (n 61), Recommendation 3.4.

64 Ibid.

65 Ibid.

66 KH Ho, *Reforming Corporate Governance in Southeast Asia: Economics, Politics, and Regulations* (Institute of Southeast Asian Studies 2005) 265.

controlled by the government, while a smaller percentage of major non-government linked companies in the banking, shipping and technology sectors are controlled indirectly through inter-corporate equity shares between government-linked and non-government linked corporations.[67]

The high concentration of ownership among company management and large shareholders often led to the creation of dual-class boards in which directors who represent significant shareholders are in a position to expropriate minority shareholders with less committed representation. While large shareholders can potentially improve the monitoring of managers because of the alignment of residual and control rights, large shareholders represent their own interests.[68] Where corporate governance is weak, large shareholders may expropriate wealth from minority investors and other stakeholders.[69]

In response to the above concern, the Steering Committee decided to impose the necessary safeguards and restrictions solely for listed companies. It therefore recommended the abolition of the entirety of section 64 from the 2006 Act and inserted section 64A to the amended Companies Act allowing public companies to issue different classes of shares subject to certain safeguards and restrictions:[70] (i) the issue of shares with differential voting rights (particularly super-voting shares) should be subject to a higher approval threshold, such as a special resolution rather than an ordinary resolution; (ii) Holders of non-voting shares should be accorded equal voting rights for a resolution to wind up the company or a resolution which varies the rights of the non-voting shares; and (iii) where there is more than one class of shares, the notice of a meeting at which a resolution is proposed to be passed should be accompanied by an explanatory statement setting out the voting rights (or lack of them) attached to each class of shares.

One main reason for the Singaporean authority allowing companies to issue different classes of shares is to help its stock exchange to compete for new listings and for the country to maintain its competitiveness as a major financial centre.[71] English football club Manchester United, controlled by the Glazer family, initially considered listing on the SGX but eventually opted to list its shares in New York in August 2012. A difficulty in obtaining approval for its DCS offer in Singapore at the time was cited as a major reason for the change in listing venue.[72]

The enactment of section 64A of its Companies Act, which came into force in early 2016, triggered a discussion between the Monetary Authority of Singapore (MAS) and the SGX whether to allow DCS listings on the latter. The Listing Advisory Committee (LAC), which is an independent committee set up in 2015 to advise SGX on listing policies,

67 PH Phan and T Yoshikawa, 'Corporate Governance in Singapore: Developments and Prognoses' (2004) Academy of International Business Annual Meeting, Research Collection, Lee Kong Chian School of Business.

68 A Shleifer and RW Vishny, 'A Survey of Corporate Governance' (1997) 52 Journal of Finance 737–83.

69 Raymond SY Chan and John KS Ho, 'Should Listed Companies Be Allowed to Adopt Dual-Class Structure in Hong Kong?' (2014) 43(2) Common Law World Review 155–82.

70 See Singapore Companies Act, s 64A for details.

71 'Singapore to Allow Dual-class Shares to Attract Listings' *Reuters* (3 October 2012).

72 Chan and Ho (n 69), at 168.

announced that it has approved the listing of DCS on the SGX in its FY2016 Annual Report.[73] Yet the specific listing rules were to be finalized after SGX completed its planned round of public consultations.

In February 2017, SGX eventually published the consultation paper regarding DCS structures[74] with the aim of drawing feedback, views and suggestions from the public regarding broad policy considerations on whether to introduce a listing framework for DCS structures in Singapore.[75] Before the publication of this consultation paper, representatives from the SGX attended a roundtable discussion with the Faculty of Law, National University of Singapore (NUS) on the future of DCS in Singapore.[76] The initial conclusion from the roundtable discussion was that these shares 'might be something worth trying as long as investors are fully aware of what they are actually buying'.[77] The roundtable discussion ended without any clear answers and solutions to the questions and problems raised on such share structures. Yet there were three key takeaways from the event:[78] (i) the safeguards, if implemented, would be unique since they are more comprehensive than elsewhere; (ii) investor awareness and education are crucial. Investors must be given the choice to invest in DCS but only during the IPO stage; and (iii) any DCS framework will be supplemented by the existing SGX one.

The SGX consultation paper of 2017 clearly stated that the concentration of control in owner managers in a company with a DCS structure carries entrenchment and expropriation risks.[79] Entrenchment risks arise when owner managers become entrenched in the management of the company. Expropriation risks arise where owner managers seek to extract excessive private benefits from the company, to the detriment of minority shareholders. In order to mitigate entrenchment and expropriation risks, the consultation paper suggested certain safeguards.[80] In order to minimize the concentration and entrenchment of voting rights in owner managers, it proposed a maximum voting differential of 10:1 and argued that this is a commonly adopted voting differential in other jurisdictions which allow the listing of dual-class shares.[81] To minimize expropriation risks, it proposed enhancing the independence element of companies with a DCS structure by requiring that if the chairman is not an independent director, at least half of the board must comprise independent directors, with a lead independent director appointed. If the chairman is independent, at least one third of the board must be independent.[82] It also proposed

73 LAC, 'FY2016 Annual Report', August 2016.

74 SGX, 'Consultation Paper—Possible Listing Framework for Dual Class Share Structures', 16 February 2017.

75 Ibid, para 1.12.

76 Michelle Dy, 'The Future of a Dual-Class Shares Structure in Singapore', Roundtable Discussion Report, Centre for Banking & Finance Law, Faculty of Law, NUS, December 2016.

77 Ibid 7.

78 Ibid.

79 SGX (n 74), 23.

80 Ibid 25.

81 Ibid.

82 Ibid.

restricting multiple vote shares to having a voting power of one vote per multiple vote share when voting on the election of independent directors.[83]

In July 2017, the SGX announced that companies with a DCS structure that is primarily listed in 'developed markets' can seek a secondary listing on the exchange.[84] It defined developed markets as any of the 22 markets the international index providers Financial Times Stock Exchange (FTSE) and Morgan Stanley Composite Index (MSCI) classify as 'developed'. All companies seeking for a secondary listing must still be subject to the listings review process and satisfy the suitability criteria. However, in a statement dated 28 July 2017, the SGX warned that approval of secondary listings of DCS companies should not be taken to suggest that a decision in favour of primary listings is a foregone conclusion.[85] Tan Boon Gin, CEO of SGX Regulations, said that DCS will provide investors with more choice, while enhancing market knowledge and familiarity with the risks and benefits of such companies.[86] On 19 January 2018, Loh Boon Chye, CEO of SGX declared that the exchange will be allowing DCS companies to be primarily listed.[87] According to Loh, the key focus of DCS is to assist companies make the transition into the new economy. In supporting the SGX's decision, the MAS said it will review the safeguards that SGX will be proposing to mitigate the risks of DCS.[88]

Since 26 June 2018, new companies seeking to list on the main board of the SGX have been allowed to offer DCS structures.[89] Almost all of the recommendations made under the SGX 2017 consultation paper were inserted into the amended rules to allow DCS structure companies for listing in order to safeguard the interests of investors. An issuer with a DCS structure must fulfil the existing admission criteria set out in Chapter 2 of the SGX main board listing rules. In addition, the issuer and the issue manager must establish that the issuer is 'suitable for listing' with a DCS structure.[90] The SGX undertakes a holistic assessment of the suitability of an issuer for listing with a DCS structure with reference to a list of suitability factors.

Having examined how the regulators in Singapore have handled the issue of DCS structure, the paper will now turn its focus to another major financial centre in the region, Hong Kong, and explore the approach adopted by the regulator in Hong Kong in handling DCS structure.

83 ibid 26.

84 The Strait Times, 'SGX clarifies on secondary listing of dual-class shares'.

85 Douglas Appell, 'Singapore's Stock Exchange gives Dual-class Shares a Secondary Listing Toehold' <http://www.pionline.com/article/20170731/ONLINE/170739996/singapores-stock-exchange-gives-dual-class-shares-a-secondary-listing-toehold> (date last accessed, 14 June 2021).

86 Ibid.

87 J Lim, 'SGX says Will Implement Dual-Class Shares' (*Channel NewsAsia*, 19 January 2018) <https://www.channelnewsasia.com/news/business/sgx-says-will-implement-dual-class-shares-9877252> (date last accessed, 14 June 2021).

88 Ibid.

89 See Ch. 7, 'Part X Dual Class Share Structure—Continuing Listing Obligations' of the SGX mainboard listing rules for details.

90 See Ch. 2 Equity Securities, Rule 210(10)(b) of the SGX main board listing rules for details.

Hong Kong

The debate on whether DCS structure companies should be allowed to list on the main board of the Hong Kong Stock Exchange (HKEx) was ignited by the Alibaba IPO incident of 2013, in which the company initially applied to list with a DCS structure.[91] The author of this article has discussed this incident extensively in the 2014[92] and 2018[93] edition of the *Common Law World Review*, it is therefore not to be repeated here again. Suffice to say that Alibaba's IPO application was eventually rejected by the HKEx, as DCS structures were prohibited under the HKEx's prior main board listing rule, LR 8.11, which stated that '(t)he share capital of a new applicant must not include shares of which the proposed voting power does not bear a reasonable relationship to the equity interest of such shares when fully paid'.

Subsequently, in March 2014, Alibaba finally decided to choose New York over Hong Kong for its IPO.[94] The company eventually filed for its IPO in May 2014[95] on the NYSE. The company managed to raise more than US$15 billion in New York, making it the highest profile listing at the time since Facebook's US$16 billion listing in 2012.

After rejecting Alibaba's IPO application, the HKEx conducted a review of its operating model and a consultation paper was published in August 2014[96] to seek views as to whether its listing rules should be changed to permit listed companies with DCS structure. In June 2015, the HKEx then published its consultation conclusions,[97] where the responses indicated support for a second stage consultation. The consultation conclusions included an outline of features of a draft proposal which the HKEx intended to refine through discussions with stakeholders before submitting it for formal consultation. The features of the draft proposal were aimed at ensuring that companies would only be allowed to list with DCS structures in certain limited circumstances and subject to a number of safeguards.[98] But on 25 June 2015, the Hong Kong Securities and Futures Commission (SFC) issued a statement and 'unanimously concluded' that it does not support the draft proposal for primary listings with DCS structures.[99] In light of this statement issued by the SFC, the HKEx in October 2015 decided not to proceed with its draft proposal to allow companies with DCS structures to list in Hong Kong.[100]

91 'Alibaba's spotlight on HK regulation' (*Webb-site*, 18 September 2013) <http://webb-site.com/articles/aligaga.asp> (date last accessed, 14 June 2021).

92 Chan and Ho (n 69) 155–82.

93 John KS Ho, 'Revisiting the Viability to Allow Dual-class Share Structure Companies to List in the Financial Market of Hong Kong' (2018) 47(3) Common Law World Review 167–95.

94 R Chan and A France-Presse, 'Alibaba Confirms it has Chosen US over Hong Kong for IPO' *South China Morning Post* (Hong Kong, 16 March 2014).

95 'Alibaba files for what could be biggest tech IPO ever' *South China Morning Post* (Hong Kong, 7 May 2014). Alibaba has implemented a special mechanism allowing founder managers to appoint a majority of the board to maintain control (Form F-1 Registration Statement, 6 May 2014).

96 HKEx, 'Concept Paper—Weighted Voting Rights' (August 2014).

97 HKEx, 'Consultation Conclusions—To Concept Paper on Weighted Voting Rights' (June 2015).

98 Ibid, Ch 5, at 44.

99 SFC, 'SFC statement on SEHK's draft proposal on weighted voting rights' (25 June 2015).

100 HKEx, 'Listing Committee Announces Way Forward on Weighted Voting Rights' (5 October 2015).

There were many reasons why the SFC objected to the proposal at the time and one of them is that under the HKEx's draft proposal, DCS structures would be limited to new listing applicants and that anti-avoidance measures would be introduced to prevent existing issuers from circumventing the prohibition on them implementing such structures. Yet the SFC questioned the effectiveness of the proposed anti-avoidance measures. To work, there needs to be mechanism to prevent existing issuers using arrangements such as spin-offs to get around the restriction.[101] As far as the SFC was concerned, this issue is particularly important for Hong Kong because similar to Singapore as discussed above, a majority of listed companies have concentrated ownership structures that are either family-controlled or state-controlled.[102] It was argued that permitting this kind of share structure may make the controlling majorities even more entrenched.[103]

However, after being shelved for two years, the discussion as to whether DCS structure companies should be allowed to list on the financial market of Hong Kong re-emerged in June 2017 with the publication of the HKEx's *Concept Paper—New Board*,[104] with the aim of reviewing its listing regime. According to the HKEx, Hong Kong has successfully established itself as an international financial centre and as a leading listing venue. HKEx had been the top IPO venue by funds raised in five of the past eight years up until 2017.[105]

Yet a review of its market structure identified gaps within its listing regime that needed to be addressed in respect of companies from 'new economy' industries in order to provide greater diversity and investment opportunities to investors in Hong Kong.[106] One major reason why Hong Kong had been the world's largest IPO venue is due to the 'mainland China' factor. The most significant financial developments in Hong Kong during the past two decades is the influx of mainland Chinese companies. From 2006 to May 2017, the concentration of mainland Chinese issuers has increased from 50.3 per cent of the market capitalization of companies listed on the HKEx to 64 per cent. During the five years ending 2016, mainland IPOs accounted for 60 per cent of the total number of IPOs in the Hong Kong market and 91 per cent of IPOs funds raised.[107] But the consequence of its success in attracting mainland Chinese companies has been a significant and growing dependence (or over-dependence) on the mainland.[108] International companies that have listed in Hong Kong in the 10 years between 2007 and 2017 accounted for only 11 per cent of the total market capitalization versus 55 per cent for the LSE and 30 per cent and 20 per

101 SFC (n 99).

102 RW Carney and TB Child, 'Changes to the Ownership and Control of East Asian Corporations between 1996 and 2008: The Primacy of Politics' (2013) 107 Journal of Financial Economics 494–513. In around 60% of publicly listed Hong Kong companies, a family controls at least 10% of voting rights. More than a third of the companies listed on the HKEx have ownerships that can be traced to mainland China and a large number of the remaining companies have close business relationships with companies in China.

103 See comment by Ashley Adler, Chief Executive Officer of the SFC, 'Opening remarks at SFC's media luncheon' (19 March 2015).

104 HKEx, 'Concept Paper—New Board' (June 2017).

105 Ibid, at 9.

106 Ibid, at 6.

107 Ibid, at 10.

108 Ibid.

cent for NYSE and NASDAQ.[109] As the Hong Kong Financial Services Development Council (FSDC) once put it, 'Although Hong Kong can be justifiably proud of its successes so far, it is still some way from its stated goal of becoming a truly international IPO centre'.[110]

Apart from a high level of dependency on mainland Chinese listings, most of the issuers listed on the HKEx are in traditional 'low-growth sectors', notably in the financial and property sectors which make up 44 per cent of its total market capitalization.[111] The biggest challenge for Hong Kong is attracting companies from new economy industries to list on its market, which in the last decade make up only 3 per cent of its market capitalization, as compared with 60 per cent and 47 per cent for NASDAQ and NYSE.[112] As a result of this, Hong Kong's market valuation in terms of price-to-earnings (P/E) ratio was the lowest among its major peers, trading at 13.4 times versus a peer group average of 24.6 times.[113] Even the HKEx admitted that its low exposure to higher growth sectors will lead to stagnation and a lack of investor interest, further depressing valuations and in turn dampening the appeal to prospective new issuers.[114]

In consideration of the drawbacks and challenges which the Hong Kong market was facing, the HKEx proposed to set up a new board to cater to the different needs and different types of issuers and investors. It originally proposed to subdivide this new board into two segments—'New Board PRO' and 'New Board PREMIUM'.[115] New Board PRO was proposed to be opened to professional investors only and New Board PREMIUM to be opened to both retail and professional investors. Both segments would allow DCS companies.[116] The justification for restricting such share structures to a new board rather than the main board, would mean that the main board would not be affected by any attempt at circumvention.[117] It would also alleviate any concern the SFC might have about allowing these companies to be listed on the main board.

However, during the consultation, the SFC backed away from its position on the one share, one vote principle.[118] Both the SFC and government wanted to see DCSs listed on the main board instead of a proposed new board, as they do not want to see a fragmented market structure.[119]

109 Ibid, at 11.
110 FSDC, 'Paper No. 9: Positioning Hong Kong as an IPO Centre of Choice' (June 2014).
111 HKEx (n 104), at 11.
112 Ibid.
113 Ibid, at 12.
114 Ibid, at 13.
115 Ibid, at 26.
116 Ibid.
117 Ibid, at 27.
118 E Yiu, 'Regulator's U-turn Paves Way for Dual-class Share Companies to Raise Funds in Hong Kong in Pilot Plan' *South China Morning Post* (27 October 2017). 'Yiu 2017' in fn 118.
119 Ibid.

During the consultation, the HKEx received responses from a broad range of respondents that were representative of all stakeholders. The responses overwhelmingly supported the need to widen the listing criteria in order to attract a more diverse range of issuers to the Hong Kong market. Yet the approach for doing so was the subject of strong debate.[120] On the issue relating to DCS structures, many respondents perceived this as a competitive issue with the risk of missing out on the listing of a large number of mainland Chinese new economy companies and how this could pose a threat to Hong Kong's position as a premier global listing venue.[121] Most respondents believed that implementing DCS should be accompanied by safeguards that provide minimum shareholder protections against long-term entrenchment of founders and against the risk of expropriation by holders of these shares.[122]

Another major controversy which the consultation exercise discussed extensively is the necessity of having a new board to accommodate DCS companies. A large number of respondents expressed concerns that the establishment of a new board would bring unnecessary complexity into the listing framework of Hong Kong and that many high quality issuers would prefer to list on the main board, making a new board less attractive.[123] As a result of the feedbacks which the HKEx received, coupled with the SFC and government attitude in preferring DCS to be listed on the main board as mentioned earlier, the HKEx concluded that instead of setting up a new board, it would insert a new chapter to its existing main board listing rules in order to cater for the needs of DCS companies.[124]

From a commercial and competition perspective, it made sense to reject the proposal of a new board to accommodate the needs of DCS companies. Lessons from the past show that setting up an alternative segment in the financial market to cater for specific companies or industrial sectors not only does not benefit the market but rather complicates matters. The Growth Enterprise Market (GEM) board which Hong Kong launched in 1999, at the height of the dot-com boom to attract listings by technology companies and start-ups is one such example. Unlike the main board, listing on the GEM does not require companies to be profitable, while main board listing candidates need to have a combined profit of HK$50 million in the three years before listing.[125] However, GEM has been a disappointment, with its turnover and market capitalization representing less than 1 per cent of the market's total. As of September 2018, there were only 383 companies listed on GEM,[126] compared with more than 2000 on the main board.[127] Therefore, in order to ensure quality listings by issuers and the long-term development of its financial market, the

120 HKEx, 'Consultation Conclusions—New Board Concept Paper' (December 2017).

121 Ibid, at 9.

122 Ibid.

123 Ibid, at 10.

124 Ibid, at 24.

125 HKEx Listing Rule 8.05 of the HKEx—'profit test'.

126 <https://www.ceicdata.com/en/hong-kong/growth-enterprise-market-gem-statistics/gem-number-of-listed-companies> (date last accessed, 14 June 2021).

127 For details on the number of the main board listings refer to the HKEx website, <www.hkex.com.hk/eng/stat/statistics.htm> (date last accessed, 14 June 2021).

HKEx decided to simply amend and insert a new chapter in its main board listing rules to accommodate DCS companies.

Furthermore, statistics from 2017 showed that the total amount of funds raised on the Hong Kong stock market dropped to its lowest level since 2007 as the city dropped to third in global IPO rankings.[128] The drop in funds raised and the slip in ranking was at least partly blamed on the fact that Hong Kong was failing to attract new technology companies, given that only 6.9 per cent of the IPO funds raised on its market were from these companies. A more detailed analysis also shows that in terms of technology IPOs, Hong Kong was only ranked tenth worldwide, behind the likes of New York, Switzerland, South Korea and Shenzhen.[129] Hence there was an urgent need for Hong Kong to diversify its financial market and appeal to prospective new issuers in order to prevent stagnation and a lack of investor interest in the long run.

With its regional arch rival, Singapore, also announcing its decision to allow companies with a DCS structure to list on its exchange in January 2018, competition for IPOs was expected to become even more intense. Therefore, instead of prohibiting companies with a DCS structure to list on its exchange, Hong Kong decided to follow in the footstep of its Singaporean counterpart by allowing these companies to list on its exchange subject to certain safeguards and restrictions.

The HKEx amended its main board listing rules and inserted Chapter 8A[130] and, since 30 April 2018, DCS structure companies have been allowed to list on its main board subject to certain safeguards and measures. Almost all the recommendations under the 2017 consultation conclusions were adopted under the new rule relating to DCS companies and only eligible persons are allowed to hold DCS. First, only new applicants are able to list with a DCS structure.[131] HKEx put in place a general anti-avoidance rule to protect shareholders from companies attempting to use artificial means to circumvent this restriction. Secondly, after listing, issuers with such a DCS will be prohibited from increasing the proportion of weighted voting rights in issue or issue any further such shares. In relation to beneficiaries of DCS, it restricts such shares to those who are (and remain as) directors of the issuer.[132] More importantly, these shares attached to a beneficiary's shares will lapse permanently if the beneficiary: (i) ceases to be a director; (ii) dies or is incapacitated; or (iii) if the shares are transferred to another person.[133] Accordingly, this is to ensure that only persons who are responsible for the issuer's performance and who owe fiduciary duties to the issuer are able to benefit from such a share structure.[134]

128 E Yiu, 'Funds Raised on Hong Kong Stock Market Fall to Lowest in a Decade' *South China Morning Post* (Hong Kong, 27 December 2017).

129 Thomson Reuters 2017.

130 HKEx Listing Rules and Guidance, Chap 8A—Weighted Voting Rights, <https://en-rules.hkex.com.hk/sites/default/files/net_file_store/HKEX4476_5103_VER10.pdf> (date last accessed, 14 June 2021).

131 Ibid, LR 8A.04.

132 Ibid, LR 8A.11.

133 Ibid, LR 8A.17.

134 HKEx (n 120), at 50–1.

Furthermore, like its Singaporean counterpart, in order to mitigate expropriation and entrenchment risks, the HKEx also require the voting power of DCS not to exceed more than 10 times of the voting power of ordinary shares and ordinary shareholders must hold at least 10 per cent of the votes.[135] Likewise, material changes to constitutional documents and variation of class rights must be decided on a one share, one vote basis.[136] In terms of disclosure, companies with such a share structure are required to be identified with a unique stock code[137](W) and appropriate warning language, rationale and associated risks must be disclosed in its listing documents.[138]

In order to further enhance investor protection, the HKEx limit applicants permitted to list with such a share structures to those companies that have an expected market capitalization of not less than HK$10 billion. The rationale is to limit applicants to established and high-profile companies that are already subject to some degree of public scrutiny. It also ensures that the economic interest in the company held by beneficiaries of dual-class shares will be large enough to align their interests with those of other shareholders. If an applicant with such a share structure has an expected market capitalization of less than HK$40 billion, the exchange will also require the applicant to have at least HK$1 billion of revenue in its most recent audited financial year.[139]

As discussed above, the reason for HKEx allowing DCS companies to list on the main board is to attract more high growth companies from hi-tech sectors as they were lacking in the Hong Kong market. Therefore, only 'innovative' companies with DCS structure are allowed to list on its exchange.[140] In its 2017 consultation conclusions, the HKEx acknowledged that it is difficult to define such companies as there is no universal definition for them and any such definition can evolve over time.[141] Hence, when the new rule on permitting DCS structure companies to list came into effect at the end of April 2018, the exchange simultaneously issued a guidance letter,[142] stipulating the factors that the exchange will take into consideration in recognizing innovative companies:[143] (i) success demonstrated to be attributable to the application of new technologies, innovations and/or business model to the company's core business which serves to differentiate the company from existing players; (ii) research and development is a significant contributor of expected value and constitutes a major activity and expense; (iii) success is demonstrated to be attributable to unique features or intellectual property; and (iv) has an outsized market capitalization or intangible asset value relative to its tangible asset value.

135 HKEx (n 130), LR 8A.09.
136 Ibid, LR 8A.24.
137 Ibid, LR 8A.42.
138 Ibid, LR 8A.37–8A.41.
139 Ibid, LR 8A.06.
140 HKEx Guidance Letter, HKEX-GL93-18, (30 April 2018).
141 HKEx (n 120), at 51.
142 Ibid.
143 HKEx Guidance Letter (n 140), at para 4.2.

As illustrated above, lessons and experiences provided by other major financial markets in the world show that the issue of whether DCS structure companies should be allowed to list remains highly controversial. Yet many exchanges allow these companies to be listed due to commercial considerations and competition pressure from rival exchanges. The USA in general adopts the most liberal approach in allowing such companies to be listed, whereas Singapore and Hong Kong take a more cautious approach by imposing safeguards and restrictions to protect investors and only allowing certain types of companies with a DCS structure to list on their main boards due to corporate governance concerns.

Having examined the experiences of other major financial markets in dealing with DCS structures, the article will now turn to examine the present treatment of DCS structure companies in the financial market of the UK and its rationales for conducting a review of its listing regime.

4. Treatment of dual class share structure companies in the UK and its recent listing regime review

According to the House of Lords ruling in *Bushell v Faith*,[144] where a company's constitutional documents already provide for weighed voting rights, shareholders are unlikely to have grounds for challenging the exercise of those weighed voting rights. Hence UK company law does not prohibit the creation of shares with unequal voting rights by companies.

Since the 1950s, the UK stock market has played an important role in the funding of public companies. Companies listed on the London Stock Exchange (LSE) had highly dispersed ownership.[145] Families owned minority stakes but had sometimes maintained control with a disproportionate representation on the board and with a DCS.[146]

Limited voting shares were widely used in the LSE and did not raise any criticisms up to the first half of the 1950s. They were considered particularly suitable for retail investors who used dividends to evaluate corporate performance.[147] One study even found that the creation of superior voting shares in the LSE was usually associated with positive price effects at the announcement.[148] It is therefore not surprising that DCS structure companies were prevalent in the UK around the mid-1960s.

Yet since the mid-1950s, comments regarding the downsides of DCS began to emerge amongst institutional investors that were starting to gain importance in the financial market. For example, in the 1956 edition of *The Economist*,[149] one argument was summarized in an article which stated that, 'Non-voting shares ought always to be regarded with

144 [1970] AC 1099.

145 J Franks, C Mayer and S Rossi, 'Ownership: Evolution and Regulation' (2009) 22 Review of Financial Studies 4009–56.

146 Ibid.

147 B Cheffins, *Corporate Ownership and Control: British Business Transformed*' (OUP 2008).

148 J Ang and W Megginson, 'Restricted Voting Shares, Ownership Structure, and the Market Value of Dual-class Firms' (1989) 12 Journal of Financial Research 301–18.

149 *The Economist*, 14 April 1956.

reserve. . . . They can put control in the hands of an irresponsible oligarchy with a minority financial stake. . . . The danger lies in the perpetuities that non-voting shareholders are powerless to control'. By the late 1950s, institutional investors developed a marked distaste and a prejudice against the undesirable practice of issuing limited voting shares. Yet the acceptance of DCS was reinstated by the Jenkins Committee, which in the early 1960s argued that it may be desirable that control is retained by insiders, especially in small family businesses. The Institute of Directors (IOD), the Board of Trade, the Institute of Secretaries and the LSE also advocated in favour of DCS at the time.[150]

However, by the early 1970s, DCS were generally viewed as an inferior claim. A report in *The Times* on 30 May 1970, reported that the pragmatic stock market view is that voting shares deserve to be rated at a premium over non-voting shares.[151] Therefore, by around 1970 most companies on the LSE had abandoned DCS structures.[152] Since then, the debate regarding the suitability of DCS on the UK financial market subsided for many decades.[153]

After the Global Financial Crisis (GFC), the UK regulator, the Financial Conduct Authority (FCA) and its predecessor, the Financial Services Authority (FSA) have introduced a series of reforms to the listing regime of its financial market. A key feature of London's listing regime in its current form is its division into two segments—Premium and Standard listing (previously known as Primary and Secondary listing). The existing two-tier segments of its listing regime came into effect in April 2010 as a result of change that was introduced in October 2009, following a review of the structure of the UK listing regime by the then FSA, with the aim of ensuring clarity of the regime's structure and issuers' obligation under it.[154]

A 'Premium listing' denotes a listing with the more stringent 'super-equivalent' standards. These standards exceed the requirements laid down in the EU Prospectus Directive and provide additional investor confidence, which in turn are considered to promote shareholder confidence.[155] A 'Standard listing' on the other hand, denotes a listing that meets EU minimum standards. Standard listing covers issuance of shares, Global Depository Receipts (GDRs), debt and securitized derivatives that are required to comply with EU minimum requirements.[156] Before October 2009, only companies incorporated outside the UK were eligible for a Standard listing. Since April 2010, Standard listings became open to all companies regardless of domicile. For the Premium listing segment, only equity shares are now eligible. Before changes were made in 2010, all equity securities were capable of having a Primary listing. Apart from equity shares, equity securities also include

150 Jenkins Committee (Report), HC Deb 28 February 1961, vol 635 cc1363-4.

151 *The Times*, 30 May 1970.

152 Ang and Megginson (n 148).

153 Cheffins (n 147).

154 J Usher, 'London IPO Options—a Premium Listing, Standard Listing or AIM?' Mayer Brown London, November 2010.

155 Ibid.

156 London Stock Exchange (LSE), Listing Regime, <http://www.londonstockexchange.com/companies-and-advisors/main-market/companies/primary-and-secondary-listing/listing-categories.htm > (date last accessed, 14 June 2021).

securities convertible into equity shares. Yet since 2010, securities convertible into equity shares, preference shares and warrants can now only have a Standard listing. Similarly, equity shares which had a Primary listing before the rule changed in April 2010 but which did not confer full voting rights do not qualify for a Premium listing on 6 April 2010. These companies were able to retain a Premium listing until 31 May 2012.

In October 2012, the FCA published another consultation paper entitled, *Enhancing the effectiveness of the Listing Regime*,[157] with its conclusions published in November 2013.[158] In broad terms, the revised rules brought under the 2012/2013 consultation are intended to increase protection for minority shareholders in premium listing companies with a controlling shareholder by:[159] (i) imposing a requirement for such companies to enter into a relationship agreement with any controlling shareholder; (ii) providing additional voting power for minority shareholders of such companies when electing independent directors; and (iii) enhancing the voting power of minority shareholders in such companies where the company wants to cancel its Premium listing.

The FCA's consultation in 2013 moved away from imposing a stand-alone requirement for issuers to control the majority of their assets to looking at control of the business as one part of a broader assessment of whether an independent business is present is helpful, as it recognized that there are a range of factors that will be relevant to this determination and this will give applicants greater flexibility in the way that they structure their business.[160] The changes in relation to voting rights of Premium listed shares re-enforce the view expressed in the 2012 consultations that issuers should not be eligible for a Premium listing where they have a share structure that allows holders of an unlisted share class to decide matters where a premium listing requires a shareholder vote. In essence, it means that companies with DCS structures are unlikely to be eligible for a Premium listing.[161] Yet companies with DCS structures may continue to list on the Standard segment.

However, in a discussion paper published by the FCA in early 2017,[162] there seemed to be a slight change in attitude towards DCS structure companies. In reviewing the existing differentiation between Premium and Standard listing, the FCA acknowledged that many stakeholders generally regard a Standard listing as an 'unattractive option' for a listing because it lacks clarity. Its purpose and obligations are unclear, while the name implies 'second best'. More importantly, advisors often tell companies not to pursue this option.[163] A number of stakeholders also raised concerns about the effectiveness of the UK's primary equity markets in providing growth capital, particularly for early stage science and

157 <http://www.fsa.gov.uk/static/pubs/cp/cp12-25.pdf> (date last accessed, 14 June 2021).

158 FCA, 'Enhancing the effectiveness of the Listing Regime: feedback to CP12/25 and further consultation on related issues', 5 November 2013.

159 Norton Rose Fulbright, 'UK Listing Regime tightened for Premium Listed companies', June 2014.

160 Ibid.

161 UK Listing Rule 7.2.1A, Premium Listing Principles 3 and 4.

162 FCA, 'Review of the Effectiveness of Primary Markets: The UK Primary Markets Landscape', Discussion Paper (DP) 17/2, February 2017.

163 Ibid, para 3.7.

technology companies. In a Green Paper published by the UK government in January 2017,[164] it noted arguments put forward by supporters of DCS structures that the enhanced voting rights they give to companies' founders allow those individuals to focus more on long-term performance and less on short-term market pressures.[165] Although the Green Paper did note that many UK-based institutional investors and shareholder representative groups have opposed such share structures due to the risk they perceive to high quality corporate governance and the interests of minority shareholders.[166]

A broader question that many stakeholders have raised is whether Standard listing is sufficiently understood or valued by issuers and investors to be effective. The 2017 discussion seeked to explore whether the current split of listing into Standard and Premium segments is too binary and could be revisited to produce more effective outcomes.[167] During the consultation, some stakeholders suggested that there should be a degree of accommodation for companies which cannot or do not wish to comply with the super-equivalent requirements of Premium listing.[168] This raised the issue of whether the listing regime should balance the need to preserve UK-style public company governance with a desire to accommodate companies from all over the world. One possibility which the 2017 discussion paper raised is the creation of an 'international segment'.[169]

The discussion paper argued that London remains a highly attractive market with a well-functioning market structure. It noted that other jurisdictions look to London as an example, and that this is partly due to development of the brand which is facilitated by Listing Rule requirements. UK's relative strength for IPOs include robust legal framework, the strength of its corporate governance requirements, the depth of capital available and the impact of index inclusion on likely analyst coverage.[170]

However, FCA's data analysis illustrates that the number of traditional secondary listings by large, established overseas companies with a primary listing in their home jurisdiction is declining. This is due to part of a long-term international trend as it becomes much easier for investors in most financial centres to trade shares in overseas companies.[171] Hence there have been very few new international issuers seeking a Standard listing of equity shares because issuers favour a GDR listing if a Premium listing is not an option. Yet GDRs are targeted at sophisticated investors and are inaccessible to many retail investors who may wish to invest in successful overseas companies.[172] Furthermore, as mentioned earlier, many issuers perceive the name of 'Standard listing' as second best and it has been reported that overseas companies are reluctant to adopt such designation.[173] In

164 Department for Business, Energy and Industrial Strategy (BEIS), 'Building our Industrial Strategy', January 2017.
165 FCA (n 162), para 1.20.
166 Ibid, para 1.21.
167 Ibid, para 1.18
168 Ibid, para 3.15.
169 Ibid, para 3.16.
170 Ibid, para 2.20.
171 Ibid, para 3.19.
172 Ibid.
173 Ibid, para 3.17.

response to this phenomenon, FCA intended to explore whether an international segment for large overseas companies would be more appropriate.

The proposal seeked to introduce a new route to UK listing for overseas companies wishing to observe higher standards of conduct without having to comply with the full suite of premium listing requirements. During the consultation, many stakeholders argued that a highly international market like the UK should be at the centre of listing activity supporting dynamic and emerging economies.[174] According to the FCA's own words, 'The rationale for having a distinct international segment is to create a new, credible listing option for large international companies which may wish to access UK markets but may feel that current UK listing requirements are not fully appropriate'.[175] This segment was believed to be attractive to companies where there is a founding family or government that wishes to retain control rights that are incompatible with a conventional Premium listing. It was proposed that such a segment would need to be clearly labelled, with a name reflecting that it is an international listing standard aimed at attracting mature and successful companies.[176] Hence it was believed that if the international segment proposal is adopted, large international companies with a DCS structure can list on this segment. Also, if introduced, the regulator would need to clearly stipulate the purpose of this segment and develop appropriate mechanisms for investor protection so as to foster market confidence.[177]

Yet the proposed international segment never came to fruition and on 19 November 2020, the UK Treasury announced a review of the UK's listing regime.[178] It is to the discussion of this that the article will now turn.

Rationales of conducting a review of the UK's listing regime

Accordingly, there are two reasons for conducting this review. First, it wants to set out a positive vision for the future of financial services in the UK.[179] Secondly, it wants the City of London to play an active part in shaping that future.[180] One issue on which the public response is being sought under the review, is whether DCS structure companies should be allowed to list on the Premium segment of the LSE?[181] Furthermore, it wanted views from the public that if DCS structure companies are allowed to list on the Premium segment of the LSE then what are the ways of ensuring London's high standards of corporate governance are maintained?[182]

174 Ibid, para 3.20.

175 Ibid para 3.21.

176 Ibid.

177 Ibid para 3.22.

178 HM Treasury, 'Policy paper—Call for Evidence—UK Listings Review' (19 November 2020) <https://www.gov.uk/government/publications/uk-listings-review/call-for-evidence-uk-listings-review> (date last accessed, 14 June 2021).

179 Ibid.

180 Ibid.

181 Ibid, Question 2.1 of the UK listings review.

182 Ibid, Question 2.3 of the UK listings review.

UK-based commentators have argued that one major reason why the UK needs to seriously consider allowing DCS structure companies to list on the Premium segment of the LSE is that, like its Hong Kong counterpart pre-2018 as discussed above, there is a lack of UK technology IPOs on the LSE in comparison to rival exchanges.[183] While the UK has been and continues to be a hotbed for science and technology companies,[184] the emergence of large, privately-owned technology companies has not been reflected in the publicly-listed sphere.[185] Figures from 2017 illustrate that the LSE has lagged behind the USA, with companies from 'new economy' industries listing on the LSE between 2007 and 2017 making up only 14 per cent of total market capitalization, compared to 60 per cent and 47 per cent on NASDAQ and the NYSE.[186]

Based on the 2017 Green Paper[187] published by the BEIS, attracting technology companies to the LSE is a policy objective in the UK[188] for two main reasons. First, equity can provide a vital source of financing for technology companies. Innovative companies with long product cycles may struggle to procure loan finance without a robust profit history. In 2016, 68 per cent of US IPOs involved pre-profit companies, rising to 75 per cent and 92 per cent of technology and bio-technology listings.[189] Technology companies seeking finance for long-term, uncertain projects may be shunned by the debt markets.[190] Hence it has been found that R&D spending can be throttled without access to the equity markets.[191] Therefore, equity financing for technology companies can have consequential benefits, encouraging innovation, productivity and growth in the economy generally.[192] Job creation will be promoted and the technology sector is predicted to become one of the largest providers of employment in the UK.[193] Furthermore, UK-based institutional investors can participate in the growth and success of technology companies if they are listed in the UK.[194] Although institutional investors can invest in technology companies listed on other exchanges, a significant proportion of investments by UK funds remains in

183 Bobby V Reddy, 'Finding the British Google: Relaxing the Prohibition of Dual-class Stock from the Premium-tier of the London Stock Exchange' (2020) 79(2) Cambridge Law Journal 315–48.

184 As of June 2019, the UK was home to 17 tech unicorns (source: A Heathman, 'London Tech Week: The Unicorn Companies at the centre of UK Tech' *Evening Standard* (Hong Kong, 10 June 2019)).

185 Reddy (n 183), at 318.

186 HKEx (n 104), at 11.

187 BEIS (n 164).

188 Ibid, at 67.

189 HKEx (n 104), at 15.

190 M Maher and T Anderson, 'Corporate Governance: Effects on Firm Performance and Economic Growth' (1999) 1 OECD 36.

191 M Bradley, G Jarrell and E Kim, 'On the Existence of an Optimal Capital Structure: Theory and Evidence' (1984) 39 The Journal of Finance 857, at 874.

192 D Cipollone, 'Risky Business: A Review of Dual Class Share Structures in Canada and a Proposal for Reform' (2012) 21 Dalhousie Journal of Legal Studies 62–92, at 69.

193 UK Tech on the Global Stage: Tech Nation Report 2019, <https://technation.io/report2019/> (date last accessed, 14 June 2021).

194 Reddy (n 183), at 319.

the UK.[195] Therefore, it makes sense for policymakers to seek methods to promote the listing of UK technology companies on the LSE.[196]

Yet, as mentioned above, since the FCA made changes to the listing regime under the 2012 consultation,[197] it is currently not possible for a listed-company to list with a DCS structure on the Premium segment.[198] Such companies can now only list on the Standard segment. But even the FCA admitted that a Standard segment listing is often considered unattractive for many potential issuers, with the very name connoting 'second best' status.[199] Also, a technology company founder could be discouraged from a Standard segment listing because these companies are excluded from the FTSE UK Index Series.[200] Financially, index-inclusion is generally associated with greater liquidity and higher share prices.[201] Hence even if a Standard listing company were to grow to a size that would otherwise be worthy of index-inclusion, it would not be able to take advantage of the associated benefits.[202]

The main reason why a technology company founder may be reluctant to list on the Premium segment that prohibits DCS structures is the fear of losing control.[203] Under a 'one share, one vote' Premium listing, a founder will lose control if it desires substantially to diversify wealth and grow the company. Yet with DCS structures, founders could pursue the benefits of a listing while retaining control, as illustrated by the rising numbers of such listings in the USA.[204] Certainly a UK technology company could list on the NASDAQ or the NYSE where DCS structures are allowed. But a foreign listing would make it more difficult for UK-based investors to share in the growth of these companies which would not be beneficial to the UK economy.[205] Moreover, neither are UK technology companies racing towards the US exchanges for listing.[206]

At its IPO in 2004, the founders of Google explicitly stated that the reason for setting up a DCS structure is to make it harder for outside parties to take over or influence the

195 Office for National Statistics, 'MQ5: Investment by Insurance Companies, Pension Funds and Trusts: October to December 2018', March 2019, at 26.

196 Reddy (n 183), at 319.

197 Above n 157.

198 UK Listing Rule 7.2.1A, Premium Listing Principles 3 and 4.

199 FCA (n 162), para 3.7.

200 The FTSE UK Index Series is a series of indices that rank UK Premium-listed companies according to various measures of performance, sometimes further sub-divided into industry sectors. The FTSE-100 for example, comprises the 100 largest UK Premium-listed companies by market capitalization.

201 Dorothy S Lund, 'Nonvoting Shares and Efficient Corporate Governance' (2019) 71 Stanford Law Review 687–745, at 711.

202 Reddy (n 183), at 326.

203 Ibid, at 327.

204 J Ritter, 'Initial Public Offerings: Dual Class IPOs', updated as of 19 December 2018, <https://site.warrington.ufl.edu/ritter/files/2019/04/IPOs2018DualClass.pdf > (date last accessed, 14 June 2021).

205 Reddy (n 183), at 327.

206 As of 31 October 2019, only three UK tech companies are listed exclusively on the NYSE—Farfetch Ltd., International Game Technology plc. and Delphi Technologies plc (source: NYSE, 'Current List of All Non-U.S. Issuers' (2019) <https://www.nyse.com/publicdocs/nyse/data/CurListofallStocks.pdf> (date last accessed, 14 June 2021)). Farfetch Ltd adopted a DCS structure at IPO.

company. A DCS structure makes it easier for the incumbent management team to follow its long-term innovative approach.[207] It is argued that the ability to take a long-term approach can particularly benefit technology companies. They are often involved in product innovation, and, especially in their early growth-phase years, seek success through the exploitation of product cycles, which can increase R&D investment at the expense of short-term profits.[208] If founders are under pressure from investors to maintain strong short-term profits, the ability of the founder to pursue such product cycles will be diminished.[209] Yet with control in the hands of shareholders who hold superior voting rights, assuming that the superior shareholders themselves have a long-term outlook, the management team can operate the business without fear that they may be removed if short-term profits are weak.[210] Moreover, the possibility that a low or moribund short-term share price can lead to predatory takeover offers by third-party acquirers is largely eroded, since a takeover can only proceed with the approval of the superior shareholders.[211]

Innovative technology companies also require the investment of 'firm-specific'[212] capital by management and employees. Managers will be more likely to invest in firm-specific human capital if they are more comfortable that their positions are secure in the long term.[213] The long-term commitment of the controller can also encourage other employees to invest in firm-specific human capital so essential in companies with high 'asset-specificity'[214] such as hi-tech industries.[215]

It is therefore argued that by allowing DCS structure companies to list on the Premium segment of the LSE enables founders to crystallize wealth and raise substantial equity capital for growth, while retaining control.[216]

Lessons and experiences from elsewhere also illustrate that by allowing DCS structure companies to list on the main board helps to attract more technology IPOs and diversify its financial market. After HKEx amended its main board listing rules in April 2018 to accommodate DCS structure companies, China's Xiaomi, the world's fifth largest smartphone manufacturer, immediately applied for its IPO on the HKEx main board in May 2018.[217] The company has a DCS structure where the shares held by co-founders Lei Jun and Lin Bin carry 10 votes each, while other shareholders get one vote per share.[218] The

207 Google Inc. Amendment No 8 to Registration Statement, 29, filed on 16 August 2004.

208 S Kupor, 'Sorry CalPERS, Dual Class Shares Are a Founder's Best Friend' Forbes CIO Network, 14 May 2013.

209 Reddy (n 183), at 329.

210 M Narayanan, 'Managerial Incentives for Short-Term Results' (1985) Journal of Finance 40, 1469–1484, at 1479.

211 Reddy (n 183), at 328.

212 In financial terms, firm-specific advantages refer to the advantages derived from specific assets, particularly intangible assets, and capabilities which bring a superior competitive position to the possessing company.

213 D Denis and D Denis, 'Majority Owner-Managers and Organizational Efficiency' (1994) 1 Journal of Corporate Finance 91, at 106.

214 Asset specificity is the degree to which an asset can be used for different purposes. High specificity means that there is little opportunity to use an asset for anything other than its initial intended purpose.

215 Reddy (n 183), at 330.

216 Ibid, at 347.

217 EUROMONEY, 'Xiaomi vindicates HK dual class decision—but at a cost', 23 May 2018.

218 Ibid.

company was eventually listed on the HKEx main board on 9 July 2018, at an implied valuation of US$54 billion.[219] Since 2018 other tech companies with DCS structures have been encouraged to list in Hong Kong, with the total valuation of these businesses at more than £23 billion.[220] Most notably, the secondary market listing by Alibaba on the HKEx in November 2019 was a further important marker in the development of the HKEx.[221] The company managed to raise more than US$11 billion in Hong Kong, making it the world's largest listing in 2019.[222] Therefore, if DCS structure companies are to be allowed to list in the Premium segment of the LSE, there is no reason why the LSE cannot replicate the success of its Hong Kong counterpart in attracting technology IPOs, given how strong the UK tech-industry is.[223]

At the time of writing, it has been reported that Amsterdam has overtaken London as Europe's largest share trading centre, and experts say the symbolic blow could be followed by the UK financial sector losing jobs as well as more businesses owing to Brexit.[224] The Dutch capital, which was previously the sixth largest exchange centre in Europe, saw average daily trading surge from 2.6 billion euro to 9.2 billion euro in January 2021.[225] This pushed London into second place, with average daily trading halving from 17.5 billion euro to 8.6 billion euro.[226] William Wright, founder of the New Financial thinktank states that UK authorities should be 'alive to the risk' that London might lose more than just trading.[227]

Therefore, there is an urgent need on the UK to diversify its listing market and appeal to prospective new issuers in order to prevent stagnation and a lack of investor interest in the long run. Instead of prohibiting companies with DCS structure to list on its Premium segment, LSE should follow the footstep of other major exchanges by allowing these companies to list, yet simultaneously impose safeguards and restrictions to ensure that high corporate governance standards can be maintained. It is this that the article will now discuss.

5. Appropriate governance measures for dual class share companies to list on the Premium segment

The conventional argument amongst corporate governance scholars is that, in financial markets dominated by listed companies with a concentrated ownership structure, such as

219 Jon Russell, 'China's Xiaomi makes Underwhelming Public Debut in Hong Kong IPO' (*TechCrunch*, 9 July 2018).

220 Pinsent Masons, 'Tech Innovators may be Swayed by Hong Kong Weighted Voting Rights Reform' (13 May 2020).

221 Reuters, 'Why is Alibaba Listing in Hong Kong?' 15 November 2019.

222 Eustance Huang, 'Alibaba Shares Surge in Hong Kong Debut, World's Largest Listing so Far in 2019' (*CNBC*, 25 November 2019).

223 Reddy (n 183), at 348.

224 Kalyeena Makortoff, 'Amsterdam Overtakes London as Europe's Top Share Trading Centre' *The Guardian* (Hong Kong, 11 February 2021).

225 Ibid.

226 Ibid.

227 Ibid.

Singapore and Hong Kong, regulators ought to be cautious in allowing DCS structure companies to list in its market.[228] This is because, in markets with concentrated share ownership structure, allowing DCS structures would increase the risk of expropriation on minority shareholders and entrenchment by controlling block-holders.[229] However, the existence of such risks has not deterred regulators in either Singapore or Hong Kong to allow DCS structure companies to list on their main boards. They have instead implemented many safeguards and restrictions after consulting with stakeholders[230] to ensure that high corporate governance standards are maintained while allowing companies with such a share structure to list. As discussed, this rationale is to attract more listings from new economy companies and enhance competitiveness vis-à-vis rival exchanges.

Yet in contrast, all academic literatures on corporate governance have long confirmed that share ownership in UK-listed companies is just as dispersed as its US counterpart.[231] One empirical study even shows that as early as the 1910s, directors in UK-listed companies routinely had control without ownership. Management was independent of securities owners and UK investors had large overseas portfolio investments.[232] When combined, these factors indicate that the majority of the corporate shares owned by UK investors were substantially divorced from managerial control, a dispersion which had happened two decades before Berle and Means[233] quantified it for the USA.[234]

Therefore, there is even less of a reason why the FCA and LSE should prohibit DCS structure companies to list on the Premium segment. Moreover, all companies with a Premium listing on the LSE are required under the Listing Rules[235] to report in their annual report and accounts on how they comply with the Corporate Governance Code (CG Code).[236] Under the CG Code, at least half of the board should be independent non-executive directors.[237] This means there are adequate checks and balances on the board to ensure that directors who hold superior voting shares do not abuse their powers.

As discussed, UK company law does not prohibit companies from creating shares with unequal voting rights[238] and at least until the mid-1960s DCS companies were prevalent on the LSE. It was merely investors' distaste of such companies after this period that led to their demise from the market.[239] The UK companies adopting such a structure at the time

228 Chan and Ho (n 92) and Ho (n 93).

229 See ibid, n 92, at 175 and ibid, n 93, at 180.

230 SGX (n 74) and HKEx (n 120).

231 Franks, Mayer and Rossi (n 145) and Cheffins (n 147).

232 J Foreman-Peck and L Hannah, 'Extreme Divorce: The Managerial Revolution in UK Companies before 1914' (2012) 65(4) The Economic History Review 1217–38.

233 Adolf A Berle, Jr and Gardiner C Means, *The Modern Corporation and Private Property* (Macmillan 1933).

234 Foreman-Peck and Hannah (n 232), at 1227.

235 FCA, LSE Premium Listing Rules, <https://www.handbook.fca.org.uk/handbook/LR/> (date last accessed, 14 June 2021).

236 UK FRC, 'The UK Corporate Governance Code 2018', July 2018, <https://www.frc.org.uk/getattachment/88bd8c45-50ea-4841-95b0-d2f4f48069a2/2018-UK-Corporate-Governance-Code-FINAL.pdf> (date last accessed, 14 June 2021).

237 Ibid, at s 2—Division of Responsibilities, para 11.

238 See *Bushell v Faith* (n 144).

239 Cheffins (n 147), at 317.

were doing so primarily to protect themselves from a burgeoning hostile takeover market and were mainly industrial and retail companies with easily observable long-term growth prospects, not redolent of contemporary, high-growth technology companies, which, as discussed, can particularly benefit from the adoption of a DCS.[240]

Although many institutional investors in the UK have in the past opposed changes allowing DCS a Premium listing in the UK, it has been reported that these same investors have invested billions in such shares in the USA.[241] It is not within the scope of this article to discuss whether these investors have been acting hypocritically but it does affirm that if UK technology companies with DCS structures are to be listed on the Premium segment of the LSE, it would be attractive for large UK investors. The article will now examine what appropriate governance measures the FCA or LSE should implement to enable DCS structure companies to list on the Premium segment by drawing experiences from other international counterparts.

Limit DCS structure for new applicants and innovative companies

First, existing listed companies on the Premium segment should not be allowed to issue superior-voting shares, as such an issuance would affect the voting rights of the existing minority shareholders who are not invited to subscribe to these shares. Prohibition of existing listed companies against the issuance of superior-voting shares can also prevent those listing companies with a single-class share structure to switch to a dual-class structure simply to benefit their controlling shareholders but at the expense of minority shareholders. This measure was implemented by both the SGX and HKEx when they amended their main board listing rules to accommodate for DCS companies.[242]

Secondly, given that it is hi-tech and new economy companies that are lacking on the Premium segment of the LSE, then, like its Hong Kong counterpart, only 'innovative companies' with DCS structures should be allowed to list on the Premium segment.[243] This makes sense because as discussed, attracting tech companies to the LSE is a policy objective in the UK.[244] Hence there is no reason why managers in the 'low-growth traditional sectors' can justify the need to hold superior voting shares to pursue their business objectives. Moreover, if a technology company conducts an IPO with DCS, the founder will be an individual that the market views as fundamental to the success of the business, and public investors will derive value from a founder with an idiosyncratic vision being bonded to the company.[245]

240 Reddy (n 183), at 335.

241 Jim Armitage, 'Fund Managers Slammed for Investing in Facebook and Google While Arguing against such Firms Listing in the FTSE 100' *Evening Standard* (13 November 2020). BlackRock, Legal & General and Columbia Threadneedle have all in the past opposed DCS companies listing on the Premium segment of the LSE. Yet all three institutions have been found to have invested billions of pounds in Facebook, Google and other US tech companies with DCS structures.

242 See Chap 7, 'Part X Dual Class Share Structure—Continuing Listing Obligations' of the Singapore's SGX mainboard listing rules for details. For Hong Kong's HKEx, see main board listing rules, LR 8A.04.

243 See HKEx Guidance Letter, HKEX-GL93-18, 30 April 2018.

244 BEIS (n 164), at 67.

245 Reddy (n 183), at 335.

Certainly, the difficulty is how to define such companies as there is no universal definition for them and any such definition can evolve over time. This is something which the HKEx was also aware of when it conducted its consultation exercise back in 2017.[246] Yet the FCA, or the LSE in the UK, can also issue guidance[247] for potential applicants, similar to what its Hong Kong counterpart has done, stipulating the factors that the exchange will take into consideration in recognizing innovative companies.[248]

Experiences from HKEx show that the regulator, in applying such guidance, can be flexible in recognizing whether an applicant is an innovative company. In September 2018, China's Meituan-Dianping, with a DCS structure, had its IPO in Hong Kong, raising US$4.2 billion.[249] The company is China's largest online food delivery-to-ticketing services and was recognized by the HKEx as meeting the criteria of an innovative company.[250] At the time of writing, UK-based Deliveroo is reportedly planning to go public and wants to adopt a DCS structure.[251] Like Meituan in China, Deliveroo is an online food delivery company founded by William Shu and Greg Orlowski in 2013 in London. Deliveroo is reportedly preparing to go public in 2021. While the UK government and LSE are keen that the listing, expected to be worth as much as £3 billion, happens in London, Deliveroo is said to be keeping New York as an option as DCS structure has long been allowed.[252] Hence, should the UK allow the listing of DCS companies on the Premium segment under the current listing review, there is no reason why companies like Deliveroo would not be recognized as an innovative company, following the example of Meituan in Hong Kong.

Another issue is whether in allowing DCS companies to list on the Premium segment of the LSE, should the regulator impose a requirement that such companies must have an expected market capitalization of a certain value or to have at least a certain level of revenue in its most recent audited financial year? When HKEx amended its main board listing rules to allow DCS companies to list, it limited applicants with such share structures to those companies that have an expected market capitalization of not less than HK$10 billion (approx. US$1.3 billion). If an applicant with such a share structure has an expected market capitalization of less than HK$40 billion, the exchange will also require the applicant to have at least HK$1 billion (approx. US$130 million) of revenue in its most recent audited financial year.[253] Yet in contrast, its rival, the SGX, did not impose such requirements in its amendment and simply stipulated that the issue manager must establish that the issuer is 'suitable for listing' with a DCS structure.[254] The SGX

246 HKEx (n 120), at 51.
247 Above (n 241).
248 Above (n 240), at para 4.2.
249 Reuters, 'Tencent-backed Meituan Raises $4.2 billion in IPO Priced near Range Top-sources' 13 September 2018.
250 Catherine Shu, 'Meituan-Dianping's IPO off to a Good Start as Shares Climb 7% on Debut' (2018) *TechCrunch*.
251 Andrew Woodman, 'UK Revisits IPO Rules to Entice Tech Founders' *PitchBook*, 19 November 2020.
252 Ibid.
253 HKEx main board listing rules, LR 8A.06.
254 See Chap 2 Equity Securities, Rule 210(10)(b) of the SGX main board listing rules for details.

undertakes a holistic assessment of the suitability of an issuer for listing with a DCS structure with reference to a list of suitability factors.

The author is of the view that the Singaporean approach on this matter is more flexible than its Hong Kong counterpart. While market capitalization and revenue can be deciding factors in considering whether an applicant is suitable for listing with a DCS structure, they should not be the determining factor. This is because evaluating the eligibility of applicants on the basis of revenue or market capitalization is perhaps too conservative given that the growth potential of many technology companies should be assessed by intangible values such as concepts or ideas. It is therefore argued that the LSE should adopt the approach of its Singaporean counterpart by undertaking a holistic assessment of the suitability of a potential DCS IPO applicant.

Limit the holding of superior voting shares to founder-managers

As discussed, one major advantage of a DCS structure for technology companies is to offer an opportunity to a founder-manager to retain control of his/her company in a rapidly changing business environment after raising capital from the public to fund an expansion project of the company. By selecting the company's management team, the founder-manager can direct his/her company to focus on its long-term strategic aims without fearing the short-termism of stock markets and the possibility of hostile takeovers by opportunistic acquirers. It follows logically from this argument that only founder-managers and current senior managers, who share a similar vision with the founder-manager, should be eligible to award the rights of subscribing superior-voting shares in those companies adopting a DCS structure.[255] These rights should only be granted to companies at their IPO.

Likewise, the HKEx also has similar requirements. In relation to beneficiaries of DCS, it restricts such shares to those who are (and remain as) directors of the issuer.[256] More importantly, these shares attached to a beneficiary's shares will lapse permanently if the beneficiary: (i) ceases to be a director; (ii) dies or is incapacitated; or (iii) if the shares are transferred to another person.[257] Accordingly, this is to ensure that only persons who are responsible for the issuer's performance and who owe fiduciary duties to the issuer are able to benefit from such share structure.[258] If shares carrying superior voting rights are transferred, the transferees must also be founder-managers who hold the same class of superior-voting shares. This article suggests that only the transfer of founder-managers' superior-voting shares to other founder-managers can preserve the superior-voting rights of the shares. Other types of transfer should automatically convert the shares to normal-voting shares with one share, one vote. Allowing the transfers of founder-managers' superior-voting shares to other founder-managers enables proper succession planning in DCS

255 B Reiter, 'Dual-class Shares: Not the Enemy' *Lexpert*, October 2010.

256 HKEx main board listing rules, LR 8A.11.

257 HKEx main board listing rules, LR 8A.17.

258 HKEx (n 120), at 50–1.

companies so that the visions and ambition of the businesses can be carried forward to a longer time horizon.

Furthermore, like its Singaporean and Hong Kong counterparts, to mitigate expropriation and entrenchment risks, the FCA or LSE should also require the voting power of DCS not to exceed more than 10 times the voting power of ordinary shares and ordinary shareholders must hold at least 10 per cent of the votes. Likewise, material changes to constitutional documents and variations of class rights must be decided on a one share, one vote basis. In terms of disclosure, companies with such a share structure should be required to be identified with a unique stock code and appropriate warning language, rationale and associated risks to be disclosed in its listing documents. Such requirements also exist under the listing rules on the SGX and HKEx when they allowed DCS companies to list on their main boards.[259]

Impose sunset provisions for the dual class share structure design

A time frame should be incorporated into the DCS structure design when a company launches its IPO. As discussed, a DCS structure is commonly adopted by a technology founder-manager to preserve control of his/her company when the company is still at an early stage of development with an unstable operating performance. After the company has been listed for some years, its operations should become more stable and it should be more capable of dealing with investors' expectations and any potential hostile takeovers. Therefore, the superior-voting shares should be terminated after the company has been listed for certain period.[260]

According to a recently conducted study which examined a dataset of corporate voting rights from 1971 to 2015 in the USA with a sample size of 9000 DCS companies,[261] it shows that young DCS companies with less than the median of 12 years from their IPOs, have about 7 per cent greater valuation than single-class share companies of the same maturity, in the same industry and year, and with similar characteristics.[262] Yet as they mature, DCS companies experience approximately 9 per cent greater declines in valuations than their single-class counterparts.[263] This evidence suggests that the costs of a DCS structure increase significantly as companies evolve, while the benefits of shielding companies from capital market pressure decrease.[264] These findings challenge the dominant view that dual-class voting is suboptimal. Rather, dual class voting is likely to be optimal for young, fast-growing companies.[265]

259 For the HKEx, see main board listing rules, LR 8A.09 to LR 8A.41 for details. For the SGX, see Chap 7, 'Part X Dual Class Share Structure—Continuing Listing Obligations and Chapter 2 Equity Securities', Rule 210(10)(b) of the SGX main board listing rules for details.

260 Above n 252.

261 H Kim and R Michaely, 'Sticking around Too Long? Dynamics of the Benefits of Dual-Class Voting' January 2019, *European Corporate Governance Institute—Finance Working Paper No. 590/2019, Swiss Finance Institute Research Paper No. 19-09.*

262 Ibid.

263 Ibid.

264 Ibid.

265 Ibid.

Therefore, rather than precluding DCS companies altogether, the study suggests that investors and companies should consider embracing dual class structures with defined sunset provisions.[266] The DCS structure could be in place until a particular event, such as the passing of a fixed period of time, triggered their retirement, or minority shareholders could vote on an extension of the structure at a predetermined time post-IPO.[267] These provisions should be simple to understand and easy to implement. They allow companies and investors to enjoy the advantages of DCS structures when those advantages are clear, that is when companies are young and growing fast, while providing a time-consistent way to dismantle them after their time is up.[268] As for the appropriate length of time which should be imposed on DCS structure design for UK companies to be listed on the Premium segment, this is something which the FCA or LSE can consult on with market participants after taking account of local market conditions.

6. Conclusion

'One share, one vote' is widely recognized as a bedrock principle of corporate governance, ensuring that directors and managers are accountable to shareholders. Controllers who hold superior-voting shares through a DCS structure will have the incentive to seek disproportionate gains and abuse those investors holding lesser-voting shares. Yet, a DCS structure could enhance the value of certain types of businesses, such as technology companies, as founder-managers can direct their businesses to focusing on long-term strategic aims.

One observation identified in the discussion of this article is that by implementing some safeguards and restrictions to maintain high corporate governance standards, like other major exchanges in the world, such companies can be allowed to list on the Premium segment of the LSE and strengthen its competitiveness in attracting IPOs of technology companies, which is currently lacking in the UK.

As financial centres face fierce external competition for businesses and investments, regulators certainly have the responsibility to frequently review regulations to ensure they are business friendly. Since Brexit from 1 January 2021, the UK's passporting capacity in financial services[269] will have to be renegotiated. The UK's adherence to a single rulebook is called into question, as exiting the EU means exiting the jurisdiction of the European Court of Justice (ECJ). Ever since the UK voted to leave the EU in 2016, there have been debates within financial circles as to whether the likes of Frankfurt, Amsterdam and Dublin[270] will eventually replace London as the next major financial centre of Europe. The

266 Ibid.

267 Ibid.

268 H Kim and R Michaely, 'Sunset Provisions for Dual-Class Share Structures' *Enterprising Investor*, 3 May 2019.

269 The EU passporting system for banks and financial services companies enables companies that are authorized in any EU or EEA state to trade freely in any other with minimal additional authorization. These passports are the foundation of the EU single market for financial services.

270 Arthur Beesley, 'Cautious Dublin reaps benefits of Brexit exodus' *Financial Times* (Hong Kong, 13 February 2019).

UK must therefore reform its listing regime and make its listing market more flexible to accommodate different companies if it wishes to maintain its competitiveness as Europe's premier financial centre.

There are, to be sure, concerns that allowing DCS companies to list in the Premium segment of the LSE may undermine investors' protection and lead to a 'race to the bottom' regulation to compete with other exchanges by relaxing listing requirements.[271] However, it is important not to jump to conclusions about the temptation of markets to compete with each other. Research conducted in the USA indicates that share prices tend to be higher for Delaware corporations than for corporations of other states, suggesting that shareholders view the lax Delaware rules as better than those of other states.[272] It is therefore confidently submitted here that due to commercial considerations, the LSE should allow DCS companies to list on the Premium segment providing there are appropriate safeguards and restrictions to protect investors.

271 Huw Jones, 'British Company Bosses Warn against "race to the bottom" in Listing Review' (*Reuters*, 6 January 2021).
272 Mark J Roe, 'Delaware's Competition' (2003) CXVII Harvard Law Review 588.