Capital Markets Policy
Financial Conduct Authority (FCA)
12 Endeavour Square
London
E20 1JN

28 July 2022

Dear Sirs

Re: FCA Discussion Paper 22-2

We are writing on behalf of the British Private Equity and Venture Capital Association, which is the industry body and public policy advocate for the private equity and venture capital industry in the UK. With a membership of over 750 firms, we represent the vast majority of all UK-based private equity and venture capital firms, as well as their professional advisers and investors. Between 2017 and 2021, BVCA members invested over £57bn into around 3,900 UK businesses, in sectors across the UK economy. Companies backed by PE/VC currently employ over 2m people in the UK and 90% of the businesses our members invest in are SMEs.

Overview of BVCA recommendations

The British Private Equity & Venture Capital Association applauds and welcomes efforts by the Financial Conduct Authority (the "FCA") and others to promote the UK as a more accessible and attractive place to do business and in particular to make the London Stock Exchange ("LSE") a more attractive listing venue. We believe that, if calibrated correctly and accompanied with other recommendations from the Lord Hill Listing Review, some of the proposals in the FCA's Discussion Paper 22/2 (the "Discussion Paper") could support the objective to improve the environment for companies to go public and the efficiency of the listing process in the UK and to attract a diverse group of global companies to list on the LSE. However, in our opinion, a number of the proposals unfortunately appear to be self-defeating in many respects, and we urge the FCA to review certain aspects of the proposals before finalising them.

Our key comments with regards to the proposals in the Discussion Paper are as follows:

- **Eligibility for FTSE indices** – It is important to note that the success of the FCA's proposals will depend largely on whether index providers, particularly the Financial Times Stock Exchange ("FTSE"), will permit issuers who opt out of the proposed supplementary continuing obligations regime to be eligible for inclusion in their indices. Until FTSE's position on the proposed single segment and two-tiered continuing obligations regime as it relates to inclusion in the indices is clear, it is difficult to provide meaningful feedback on the FCA's proposals. We urge the FCA to engage in discussions with FTSE so that market participants receive a clear answer at this stage of the consultation process and can be further consulted for fully-informed feedback on the proposals in light of FTSE's position before the reforms are finalised.

- **Single segment** – It may not be appropriate to expect all issuers to adhere to the requirements of the proposed single segment, such as engaging a sponsor, complying or explaining against the UK Corporate Governance Code, complying with the Premium Listing Principles (if extended as proposed) and losing the flexibility to introduce weighted voting rights. The eligibility requirements for a standard listing reflect the historical minimum EU directive standards, which can still be seen in the European market and provides issuers of equity securities with greater listing flexibility than the proposed future regime that, with its heightened standards, could result in the LSE looking less attractive to issuers in comparison to other European markets. Certain issuers, for example tech start ups and early growth companies, typically have a dual share structure, which is currently allowed for standard segment listed issuers. Removing the standard segment and imposing premium eligibility requirements on the proposed single segment could reduce potentially the attractiveness of the LSE for tech start-ups and other early growth companies. Furthermore, some of the proposed requirements of a single segment would increase the costs of listing for prospective issuers and may as a result discourage listing on the LSE. The single segment as currently proposed in the Discussion Paper may, therefore, not have the desired effect of broadening access to a wider pool of issuers.

- **Depositary receipts** – It is our view that depositary receipts should be eligible for listing on the proposed single segment. Depositary receipts represent the underlying shares of issuers and holders have the right to the underlying shares. Given that the stated aim of the proposals is to simplify the equity listing regime, it is unclear why a two-tier regime for equity securities is being retained.

- **Retail investors** – The FCA should consider whether its proposals will increase retail participation in light of its review of the Secondary Capital Raising regime, which is aiming to increase the attractiveness of investment by retail investors.

- **Class 1 transactions** – It is our view that there are strong arguments in favour of raising the level of the threshold for Class 1 transactions within the significant transactions regime. An increase of the threshold from 25% to 33% would result in a significant number of UK issuers becoming more competitive in M&A processes.

- **Sponsor regime** – Given that many non-UK listing venues, such as Nasdaq and other EU jurisdictions, do not have a sponsor regime, we believe the FCA should explore whether the sponsor regime should be retained for the proposed single segment. However, if the sponsor regime is to be retained, we urge the FCA to explore the introduction of sponsor guidelines and new disclosure requirements relating to sponsor fees.

We have limited our responses to the FCA's questions in the Discussion Paper to those questions we believe are particularly relevant to our members.

BVCA responses to the Discussion Paper questions

Chapter 3: The structure of the listing regime

Q1. Do you think that a single segment regime would meet the outcomes we have described? Are there any changes or enhancements that could be included to enhance the effectiveness of a future regime?

FTSE Indexation:

In our opinion, the effectiveness of the proposals will depend largely on whether issuers who opt out of the proposed supplementary continuing obligations regime will be eligible for inclusion in the FTSE indices, or whether FTSE will require issuers to opt in to the supplementary continuing obligations regime as a condition to being included in its indices. If the latter, the proposals would not mark a material departure from the approach to FTSE index inclusion under the current standard/premium segment regime. Some issuers seeking FTSE index inclusion may be unable or unwilling to adopt the supplementary continuing obligations and so, if FTSE were to insist on supplementary continuing obligations as a condition for inclusion on its indices, the proposed single segment is unlikely to achieve the goal of broadening access to listing.

Given the importance of FTSE index inclusion for many issuers seeking a UK listing, we are unable to provide meaningful feedback on the FCA's proposals without having visibility on FTSE's approach to indexation under the proposed future regime. FTSE needs to provide a clear answer on whether issuers who do not adopt the supplementary continuing obligations will be eligible to index inclusion as soon as possible, and in any event before the FCA publishes its final listing rules. While we recognise that the FCA does not have the jurisdiction to determine the eligibility requirements for inclusion in FTSE's indices, we strongly encourage the FCA to clarify with FTSE their position before the final listing rules of the proposed future regime are finalised and published.

Eligibility Requirements:

Subject to FTSE's position on indexation eligibility, we are in principle in favour of the proposed single segment for equity securities. Companies typically prefer the gold-plated standards of the premium segment to list their shares, which suggests that most issuers either do not consider the current premium eligibility requirements to be a barrier to listing or, to the extent that they are unable to meet the premium eligibility requirements, decide to list on an alternative market in lieu of a standard listing. However, under the FCA's proposals, the standard segment would still remain for, amongst others, secondary listings and global depositary receipts. Given that the stated aim of the proposals is to simplify the equity listing regime, it is unclear why a two-tier regime for equity securities is being retained. See also our response to Question 11 below.

Notwithstanding the above, there is a concern that the single segment as currently proposed, while looking to attract more issuers, could actually create a greater barrier to listing on the London Stock Exchange for some issuers. The eligibility requirements for a standard listing reflect the historical minimum EU directive standards, which can still be seen in the European market and provide issuers of equity securities with greater listing flexibility than the proposed future regime. We note that there is nothing that is inherently disadvantageous with a two-tier or multi-tier regime. For instance, the Nasdaq Stock Market ("Nasdaq") market operates three distinct segments, with both equity shares and depositary receipts eligible for listing on the same market segment of Nasdaq.

Q2. Do you agree that revenue track record, historical financial information and the requirement for a 'clean' working capital statement can be replaced by disclosure in listing documentation such as prospectuses?

A disclosure-based approach would provide greater accessibility for issuers, especially high-growth companies, while still protecting investors as they would be able to decide whether or not to invest based on the disclosures made by an issuer. These changes are likely to be welcomed by issuers, particularly small science and early-stage technology companies, as well as companies that are highly acquisitive, which are typically unable to satisfy the current revenue earning track-record requirements.

Given that other listing venues outside the UK are considered to be more attractive to technology and early growth companies in light of their flexible listing regimes, it would make sense to introduce more flexible disclosure and eligibility requirements that would benefit companies in the technology sector. By way of an example, on the Hong Kong Stock Exchange (the "HKSE"), biotech companies that are unable to satisfy the three regular financial requirement tests may be subject to, amongst others, additional disclosure requirements relating to the relevant experience of their directors and senior management in the commercialisation, manufacturing, development and research of biotech products.

Alternatively, access could also be broadened by having an expanded set of financial criteria or exceptions, allowing for different ways to meet them. For example, there are four sets of alternative entry standards to the Nasdaq Global Select Market based on earnings, capitalisation with cash flow, capitalisation with revenue and assets with equity. However, given that the Discussion Paper notes that the FCA lacks the expertise to formulate a greater set of financial eligibility criteria, we are in favour of the Discussion Paper's recommendation to move to a disclosure-based model instead of prescribing such additional financial eligibility criteria.

Q3. Under a disclosure-based regime, are there any elements of the listing regime that should be incorporated into future changes to the prospectus regime to ensure that investors receive appropriate information upon which to base their investment decisions?

Given that the UK Prospectus Regulation already prescribes three years' accounts (if available), complex financial history and significant financial commitment requirements, as well as a general duty of disclosure requiring any other information necessary for an investor to make an informed assessment, we consider such requirements to be sufficient for investors to be able to make their investment decisions. However, to the extent that alternative disclosure requirements are introduced to the listing regime for certain types of issuers that are unable to provide historical financials (e.g., similar to the HKSE regime for biotech companies as discussed in Question 2 above), then such disclosure requirements should also be incorporated into future changes to the prospectus regime.

Q4. Do you agree with extending the Premium Listing Principles to all issuers of equity shares in commercial companies under a single segment regime? Would any specific changes to the principles be necessary to do so?

Not all commercial companies would wish to, or be able to, adhere to all of the Premium Listing Principles, particularly in the case of non-English companies that are subject to different local law requirements. That said, to ensure uniformity and high governance standards, we think that a number of the premium listing principles could be extended to all issuers of equity shares listed on the single segment, specifically those Principles that relate to the equal treatment of investors.

Q5. Do you agree that we should consider allowing dual class structures in the single segment? Do you agree that the only form of dual class structure that should be permitted within a single segment regime should be the regime recently introduced in PS21/22?

As the FCA has recognised, replicating the dual class share eligibility requirements that currently apply to the premium segment for the proposed single segment could restrict some of the flexibility that applies to the current standard regime.

Each of Deliveroo and Wise, which both operate dual class structures, opted for a standard listing. By removing the standard segment and imposing premium eligibility requirements on the proposed single segment, this could reduce flexibility for tech start-ups and other early growth companies and make the LSE less attractive as a listing venue. A single segment with dual class share structure rules based on the current rules applying to the premium segment would mean that such companies would still not be able to list.

Whilst it is important to expand London's accessibility for fast-growing tech companies, we think greater priority should be given to maintaining London's reputation for high standards of corporate governance. In light of that, while we do not have any particular concerns with the proposed 20:1 ratio for weighted voting rights introduced in PS21/22, we note that the HKSE rules stipulate a maximum ratio of 10:1, which is also what is commonly seen in the U.S., and so we encourage the FCA to consider further the appropriate ratio.

Q6. Do you think the eligibility requirements for the single segment regime described will broaden access to listing to a wider range of companies?

Yes. In our view, the eligibility requirements for the proposed single segment coupled with a disclosure-based approach would broaden issuer access to listing. In particular, the removal of the requirement for a financial track record would make London more accessible for early stage growth companies.

However, as noted in Question 5 above, founders of early stage growth companies often prefer to structure and maintain a dual class share structure for their company and may, as a result, consider other listing venues to be more attractive than the proposed single segment (for example, Alphabet, Meta, Zoom, Airbnb and Snap all have a dual class share structure and have opted to list in the U.S.). In addition, an increase in the number of continuing obligations, even for issuers adopting only the proposed mandatory obligations, may deter companies that may previously have considered listing on the standard segment from a London listing under the proposed future regime.

Q7. Does the suggested division between the mandatory and supplementary continuing obligations provide enough flexibility for issuers, alongside appropriate investor protection? Please provide any evidence and examples where possible.

We think it is appropriate to give issuers a choice in their level of continuing obligations. That said, whilst issuers will have greater flexibility on paper (although the minimum requirements have effectively been raised for all issuers under the proposed future regime), they may find the flexibility to be limited in practice. As previously noted, the key point is the index providers' position on continuing obligations as a requirement for inclusion onto their indices.

Q8. Should more be done to ensure there is a genuine choice for issuers to decide whether the supplementary continuing obligations are suited to their business model and strategy?

Yes. As prefaced, any "genuine choice" is in any case likely to depend on what requirements FTSE may specify for inclusion onto its indices. See Question 1.

Q9. What sort of labelling would be most helpful to ensure investors are aware of whether an issuer is opted into the supplementary continuing obligations? E.g. Annual reports, noted on the Official List, or made clear by the trading venue.

We consider that such labelling should be included on each of the website of the relevant trading venue, the issuer's annual report and the Official List.

Q10. What factors should we take into account when considering the level of the threshold for Class 1 transactions within the significant transactions regime? What threshold would be appropriate?

Under the current class tests regime, given the requirement to obtain shareholder approval for Class 1 transactions, the relatively low 25% threshold has left UK premium listed companies at a disadvantage in auction bidding against private companies and overseas companies that are subject to less stringent requirements. In addition to the lack of competiveness of UK premium listed companies in competitive M&A processes, the length of time required to obtain shareholder approval and the increase in cost (both due the shareholder approval process and the potential for having to pay a premium on the purchase price to offset the added risk of a shareholder vote) has resulted in the LSE being considered to be an unattractive listing venue for companies whose strategy relies on regular acquisitive activity.

We would, therefore, be in favour of increasing the threshold for class 1 transactions from 25% to 33% to reduce the number of UK companies that would trigger the Class 1 transaction threshold, thereby increasing their competitiveness in auction processes, as well as promoting the UK as a more attractive option for a broader type of issuer.

Q11. Do you consider the scope of the single segment to be appropriate? Should any additional instruments be eligible to list there? E.g. Depositary Receipts (DRs)

In our view, depositary receipts should be eligible for listing on the proposed single segment. Depositary receipts represent shares and the holder is entitled at any time to withdraw their underlying shares, and we do not see a reason why they should be differentiated in a single segment regime. Certain overseas jurisdictions, such as Cyprus, do not allow for the listing of shares on an overseas trading venue, thus if they want to list, they can only list depositary receipts to gain access to international investors in equity markets. If an issuer with depositary receipts can meet the mandatory disclosure requirements of the proposed single segment, which presumably some of them would, then those should be permitted access to the proposed single segment. This would bring the UK listing regime in line with Nasdaq, which currently permits both shares and depositary receipts to be listed on the same segment.

Aside from depositary receipts, it may also be difficult for special purpose acquisition companies ("SPACs") to meet the eligibility requirements of the proposed single segment. However, whether or not the single segment should do more to attract SPACs is to be considered in light of market trends and whether SPAC listings are likely to be a continuing force.

Q12. Do you think the current regime for listing closed ended investment funds is fit for purpose?

We believe that any changes to LR 6, to the extent relevant (such as the removal of the requirement for unqualified working capital), could be reflected in the listing criteria for closed ended investment funds.

Q13. Do you agree that 'UK listing' could be used to describe the possible regime described?

We are in favour of describing the proposed regime as a "UK listing", though we think it is likely that most market participants will continue to refer to a "London listing".

Q14. Are there any other factors we should take into account when considering the treatment of existing standard listing issuers?

Please note our comments on depositary receipts in Question 11.

Q15. What transition arrangements should we put in place for premium listed companies in order to optimise the benefits of a single segment regime?

As noted previously, much of the success of the FCA's proposals will hinge on the index providers' position on the proposals and how those relate to inclusion in their indices. The FCA would need to ensure that index providers give clear information on what issuers would need to do in order to remain on their indices, such information to be provided to issuers with adequate advance notice to give issuers sufficient time to implement any changes to their corporate governance structures.

Chapter 4: The sponsor regime - forward looking approach

Q21. Would more transparency of how sponsor fees are calculated help issuers and investors to better understand sponsor services and the role of a sponsor?

Yes. Outside of the listing context, the UK Takeover Code requires detailed disclosures of advisor fees and the general consensus is that such disclosures are not detrimental to advisors.

Q22. Would it also help to be able to differentiate more clearly between the sponsor services and non-sponsor services that may be provided by the same provider? How might this clearer differentiation be achieved?

In IPOs, sponsor fees are often included in the underwriting commission arrangements rather than being a standalone cost. However, we believe the market would benefit from greater disclosure and transparency of sponsor fees.

Q23. What more could be done to better align a sponsor's incentives with the long-term interests of an issuer, and the interests of investors, to seek to maximise the benefits to be gained from the sponsor regime? Is there more information regarding the performance of a sponsor and of the performance of an issuer, at IPO and thereafter, that could be used to demonstrate this?

Since the sponsor plays a dual role in guiding issuers through the listing process and maintaining market standards so that investors are protected, linking sponsor fees to the success of the transaction could create a perception that there is a conflict of interest. We encourage the FCA to explore alternative fee arrangements that would not result in a potential conflict of interest arising.

In addition, we are in favour of greater disclosure of sponsor fees in listings to greater protect the interests of the issuer and its investors. For example, in Hong Kong, the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission (the "SFC") stipulates that sponsor fees should be clearly specified in every mandate letter, including the basis on which the fee is determined, the payment structure and timing and any other factors affecting fees. The FCA should consider adopting a similar disclosure requirement for sponsor fees in UK listings.

Q24. Are there any specific modifications to the role of the sponsor that you think would be needed, if the sponsor regime were applied to all issuers of equity shares in commercial companies under a single segment? For example, are there risks that may arise from longer periods of time between sponsor engagement with a company and the provision of assurances to the FCA and, of so, how might they be mitigated?

If the sponsor regime were to apply to all issuers of equity shares in commercial companies under the proposed single segment regime, this could be an additional burden and cost for those issuers who would have previously listed on the standard segment under the current regime. It is important that the FCA consider the financial consequence of applying the sponsor regime to all prospective issuers. That said, we note that Hong Kong is seen as an attractive listing venue for issuers despite the fact that it imposes a blanket requirement to appoint a sponsor for both its premium and standard listing regimes.

In Hong Kong, the sponsor must have completed all reasonable due diligence on the issuer before the listing application form is submitted and the SFC will publicly name and shame issuers and their sponsors if the supporting documentation is deficient. This approach was adopted after extensive consultation with market stakeholders. In addition, Hong Kong sponsors have access to the Hong Kong Sponsor Due Diligence Guidelines, which contain over 700 pages of guidance on the duties of sponsors (put together by leading Hong Kong law firms, banks and corporate advisory businesses).

While UK sponsors vet an issuer's eligibility for a premium listing as part of their role, given the proposed expansion of the sponsor regime to a wider range of issuers and the greater role for sponsors under the proposed single segment, the FCA should consider expanding LR 8 to provide more clarity on the sponsor's role or alternatively explore the option of introducing guidance similar to the Hong Kong Sponsor Due Diligence Guidelines.

Q26. Are there other circumstances in which the sponsor regime should be extended/applied more widely? For example, to any other issues of securities currently listed in the standard listing segment.

We would not be in favour of extending the sponsor regime. Whilst investors and the FCA might benefit from an extension of the sponsor regime to cover other issuers or other types of securities, this may be overly burdensome for sponsors and issuers. Again, the financial consequence on prospective issuers of any widening of the sponsor regime should be carefully considered. Conversely, to extend the sponsor regime, the FCA may have to reduce certain duties and responsibilities of sponsors in relation to the additional types of listings, which may not be an attractive path to go down.

British Private Equity & Venture Capital Association
3rd Floor, 48 Chancery Lane, London WC2A 1JF
+44 (0)20 7492 0400 | bvca@bvca.co.uk | www.bvca.co.uk

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

Yours faithfully,

Gurpreet Manku

Deputy Director General & Director of Policy, British Private Equity & Venture Capital Association