

February 17, 2021

The Right Hon. Lord Hill  
The Right Hon. Rishi Sunak, MP, Chancellor  
HM Treasury,  
1 Horse Guards Road London  
SW1A 2HQ  
United Kingdom

Via email: [ListingsReview@hmtreasury.gov.uk](mailto:ListingsReview@hmtreasury.gov.uk)

Via email: [Karis.Alpcan@hmtreasury.gov.uk](mailto:Karis.Alpcan@hmtreasury.gov.uk)

Re: Call for Evidence- U.K. Listings Review

Dear Lord Hill and Mr. Sunak:

I am writing on behalf of the Council of Institutional Investors (CII), a nonprofit, nonpartisan association of U.S. public, corporate and union employee benefit funds, other employee benefit plans, state and local entities charged with investing public assets, and foundations and endowments with combined assets under management of approximately \$4 trillion. Our member funds include major long-term shareowners with a duty to protect the retirement savings of millions of workers and their families, including public pension funds with more than 15 million participants. Our associate members include non-U.S. asset owners with about \$4 trillion in assets, and a range of asset managers with more than \$35 trillion in assets under management.<sup>1</sup> CII members have significant capital invested in the U.K., and we share a commitment to healthy public capital markets around the world and strong corporate governance.

We understand that the independent review of the U.K. listings regime is ongoing and that this review includes an examination of current rules on dual-class share structures (DCSS).<sup>2</sup> We agree that “the review should pay the highest regard to London’s reputation as a world-class market for company listings that promotes high standards of corporate governance, shareholder rights and transparency.”<sup>3</sup> We write to oppose any expansion of dual-class share offerings, which we believe would be inconsistent with this goal, and to urge that any expansion of DCSS on U.K. exchanges be accompanied by listing requirements ensuring that companies with unequal voting rights convert to equal voting rights on or before the seventh anniversary of their initial public offering or direct listing on the public markets.

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<sup>1</sup> For more information about the Council of Institutional Investors (CII), including its board and members, please visit CII’s website at <http://www.cii.org>.

<sup>2</sup> Terms of Reference: Lord Hill’s review on listings, November 2020, <https://www.gov.uk/government/publications/uk-listings-review/terms-of-reference-lord-hills-review-on-listings>; Call for Evidence- UK Listings Review, November 2020, <https://www.gov.uk/government/publications/uk-listings-review/call-for-evidence-uk-listings-review>

<sup>3</sup> *Id.*

## Reasons to Oppose Dual Class Share Structures

Since CII's founding in 1985, our member-approved policies have supported the principle of "one share, one vote": Every share of a public company's common stock should have equal voting rights.<sup>4</sup> Since then, as more companies have gone public with unequal voting rights, global competition has continued to erode corporate governance standards. While we acknowledge the prominent role U.S. stock exchanges have played in that erosion, we urge the U.K. to avoid yielding to this "race to the bottom" pressure, which presents a meaningful risk to long-term performance and could have reputational risks for the U.K. financial markets which are respected worldwide for maintaining high global standards.

We agree with cited concerns that "allowing companies to issue shares without equal voting rights risks eroding corporate governance standards and unfairly impinges upon shareholders rights."<sup>5</sup> Our primary concern with the expansion of dual-class shares is the principal-agent risk that is exacerbated for investors when equity structures skew the alignment of ownership and voting rights. Fundamentally, CII believes that when a company goes to the capital markets to raise money from the public, equity investors with the same residual claims should have equal protections and rights, including the right to vote in proportion to the size of their holdings.

## Academic Evidence

CII's concerns over unequal voting rights are supported by a growing body of empirical research that shows that negative effects of unequal voting rights tend to develop in the medium to long-term. In recent years, some new companies with dynamic leadership and innovative ideas that have unequal voting rights have attracted capital on public markets with limited apparent valuation discount in the immediate period after the initial public offering (IPO), even though insiders hold super-voting shares. But over time, and on average, the valuation of these firms tends to decline.

Numerous studies show that as the "wedge" between ownership and control widens, the agency costs of insider control and lack of shareholder accountability increase, founders' entrepreneurial skills and insights that initially propelled a company become dated, and opportunities and risks change in ways not foreseeable by investors at IPO.<sup>6</sup> This body of research includes:

- A study from Harvard Law School researchers Lucian A. Bebchuk and Kobi Kastiel that indicates that the benefits of multi-class structures can be expected to decline, and the costs to rise, over time.<sup>7</sup>

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<sup>4</sup> CII Policies, "Shareowner Voting Rights," [https://www.cii.org/corp\\_gov\\_policies#shareowner\\_rights](https://www.cii.org/corp_gov_policies#shareowner_rights)

<sup>5</sup> Call for Evidence- UK Listings Review, Nov. 2020, <https://www.gov.uk/government/publications/uk-listings-review/call-for-evidence-uk-listings-review/>

<sup>6</sup> See CII summary of six studies at <https://www.cii.org/files/CII%20Summary%20of%20DC%20Studies.pdf>.

<sup>7</sup> Lucian A. Bebchuk and Kobi Kastiel, "The Untenable Case for Perpetual Dual-Class Stock," 103 Va. L. Rev. 585-631 (June 2017), available at [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2954630](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2954630).

- A study from the European Corporate Governance Institute that shows that even at innovative companies where multi-class structures correlate to a value premium at the time of the IPO, that premium dissipates within six to nine years before turning negative.<sup>8</sup>
- A study from Lindsay Baran, Arno Forst and M. Tony Via that finds that multi-class structures correlate with more innovation and value creation in the period shortly after an IPO, but within six to 10 years, the costs of unequal voting structures come to outweigh the benefits.<sup>9</sup>
- A study from Robert Jackson Jr., former commissioner at the U.S. Securities and Exchange Commission, that finds that by seven years after IPO, perpetual multi-class firms exhibit valuations that are significantly lower than firms with “sunset” provisions.<sup>10</sup>
- A study from the European Corporate Governance Institute (ECGI) and the Swiss Finance Institute that finds a similar result, as multi-class structures become increasingly value destroying by 11 years after IPO.<sup>11</sup>

### Time-Based Sunsets

We recognize that shareholder voting rights can be perceived by some founders as creating negative short-term pressure in some circumstances, and that there may be pressures in the U.K. to expand DCSS to attract “fast-growing new economy companies.”<sup>12</sup> In this context, should you decide to recommend that DCSS be allowed in the Premium Segment of the London Stock Exchange, we urge you to consider mitigating long-term investor risks by supporting a mandatory time-defined sunset on unequal voting rights of no more than seven years. As shown above, the body of empirical research indicates that any benefits of holding dual-class stock decline over time, with companies with dual-class shares eventually tending to be undervalued as compared to their peers around this time.<sup>13</sup> Moreover, as a key study demonstrates, “controllers have perverse incentives to retain dual-class structures even when those structures become inefficient over time.”<sup>14</sup> This makes it difficult for dual-class companies to ever regain alignment of ownership and voting rights unless there are time-based sunsets in place.

We note it is not just empirical evidence that supports reasonable time-based sunsets; a growing number of companies that go public in the United States with differential voting rights are

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<sup>8</sup> Martijn Cremers, Beni Lauterbach and Anete Pajuste, “The Life Cycle of Dual-Class Firms,” at [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3062895](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3062895)

<sup>9</sup> Lindsay Baran, Arno Forst and M. Tony Via, “Dual Class Share Structure and Innovation,” at [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3183517](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3183517)

<sup>10</sup> Robert Jackson, “Perpetual Dual-Class Stock: the Case Against Corporate Royalty,” at <https://www.sec.gov/files/case-against-corporate-royalty-data-appendix.pdf>

<sup>11</sup> Hyunseob Kim and Roni Michaely, “Sticking Around Too Long? Dynamics of the Benefits of Dual-Class Structures,” at [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3145209](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3145209).

<sup>12</sup> Terms of Reference: Lord Hill’s review on listings, November 2020, <https://www.gov.uk/government/publications/uk-listings-review/terms-of-reference-lord-hills-review-on-listings>

<sup>13</sup> See CII summary of six studies; See Lindsay Baran, Arno Forst and M. Tony Via, “Dual Class Share Structure and Innovation,” at [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3183517](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3183517) (“[o]ur findings lend credence to the recent call from shareholder advocacy groups that if dual class structures should be allowed at all, they should face rigorous sunset provisions and be eliminated in a certain period post-IPO.”)

<sup>14</sup> See Bebchuk and Kastiel. Founders and insiders with super-voting rights have strong incentives to retain multi-class structures even after they become inefficient, and investors cannot rely exclusively on private ordering to eliminate multi-class structures that become inefficient with time.

incorporating time-based sunsets into those structures.<sup>15</sup> For these reasons, we believe that any listing rules that allow dual-class stock should also include mandatory time-based sunsets, regardless of premium or non-premium status.

Thank you for considering our views. We believe that decisions made by the U.K. government are consequential not only for companies listed on the London Stock Exchange but also more broadly in the region and globally. As such, we appreciate this review process before reaching any decisions. If we can answer any questions or provide additional information on this matter, please do not hesitate to contact me at +1.202.261.7082 or [amy@cii.org](mailto:amy@cii.org).

Sincerely,

A handwritten signature in blue ink that reads "Amy Borrus". The signature is fluid and cursive, with a long horizontal stroke at the end.

Amy Borrus  
Executive Director

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<sup>15</sup> CII's list of Companies with Time-Based Sunsets on Dual-Class Stock, <https://www.cii.org/files/12-14-20%20Time-based%20Sunsets.pdf>.