PENSIONS AND
LIFETIME SAVINGS
ASSOCIATION

14 September 2021

Capital Markets Policy
Financial Conduct Authority
12 Endeavour Square
London
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Email: cp21-21@fca.org.uk

Dear Sir/Madam,

Primary Markets Effectiveness Review

We welcome the opportunity to respond to this consultation. Below we have set out some comments in relation to some of the specific proposals in this consultation, mainly dual class share structures (DCSS) and free float requirements. Please note, that we have not commented on the various models explored in Section 3 of the paper.

About the PLSA

The Pensions and Lifetime Savings Association brings together the pensions industry and other parties to raise standards, share best practice, and support our members. We represent over 1,300 pension schemes with 20 million members and £1 trillion in assets, across master trusts and defined benefit, defined contribution, and local government schemes. Our members also include some 400 businesses which provide essential services and advice to UK pensions providers. Our mission is to help everyone to achieve a better income in retirement. We work to get more people and money into retirement savings, to get more value out of those savings, and to build the confidence and understanding of savers.

Response

Dual Class Share Structures

The PLSA has previously expressed concern about any move away from the fundamental principle that voting rights should be directly linked to a shareholder's stake in a company[1]. We remain of the view that this principle is essential in maintaining the high corporate governance standards with which the UK has long been associated, as well as in acting as a protector of minority

[1] https://www.plsa.co.uk/Policy-and-Research/Document-library/UK-listings-review-call-for-evidence-PLSA-response

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shareholders. We therefore do not support the proposals put forward that would enable the introduction of weighted shares for the first time in UK premium listed companies *(Q18)*.

As you may be aware, the pensions sector is currently undergoing period of unprecedented scrutiny in relation to stewardship of assets, both from pension savers increasingly aware of the impact of climate change, and from the UK Government. The PLSA welcomes this drive – we believe that the effective stewardship is vital in protecting the pension pots of UK savers over the long term, and we recognize the importance of scrutiny of ESG themes. Indeed, we seek to be proactive in supporting our members in their stewardship activities wherever we can, including promoting membership of the FRC Stewardship Code since its launch in 2010[2], and working with the Investment Association to find solutions to more effective stewardship[3]. This is in addition to a number of Government lead initiatives seeking to promote (or mandate) more active stewardship. In the coming months, the largest pension schemes will be required to produce Taskforce for Climate Related Financial Disclosure reports[4], a significant step in ensuring effective scrutiny of climate change, and one which will require trustees to demonstrate how they are managing risks within their investment portfolio. Over the coming years, it is likely that this requirement will be extended to all pension schemes, including smaller schemes[5].

As you will appreciate, the sector is therefore extremely apprehensive about any measured that will reduce the ability of investors – particularly minority shareholders – to influence companies, and to hold them to account, in relation to these matters. We note the premise in the consultation paper that the corresponding changes to market capitalization rules will offer additional protections to investors by increasing liquidity, and therefore reducing the risk of a fluctuating share price. However, as responsible investors we would note our concerns that the paper does not reflect on the ability of investors to, for example, secure climate change commitments, or positively influence matters of diversity. As long-term responsible investors, pension schemes have a long history of working in collaboration with other asset owners, managers and stakeholders to ensure long term value creation in the interests of savers via a variety of engagement tools[6]. Voting rights have proven to be an effective tool to do so, and we remain concerned that, even with the protections put forward, some of these proposals will fundamentally weaken those abilities. We do not believe this is in the interests of pensions savers, nor is it in keeping with the wider policy agenda on stewardship of assets.

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[2] https://www.plsa.co.uk/Policy-and-Research/Stewardship/Corporate-Governance-and-investment-stewardship-policy-reform

[3] https://www.theia.org/media/press-releases/pension-funds-and-investment-managers-join-forces-better-embed-stewardship

[4] https://www.gov.uk/government/consultations/taking-action-on-climate-risk-improving-governance-and-reporting-by-occupational-pension-schemes-response-and-consultation-on-regulations/taking-action-on-climate-risk-improving-governance-and-reporting-by-occupational-pension-schemes

[5] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/933783/FINAL_TCFD_ROADMAP.pdf

[6] https://shareaction.org/wp-content/uploads/2021/04/Investor-letter-to-Barclays-regarding-its-energy-policy-26.04.2021.pdf

Nevertheless, we appreciate that many of the protections set out in the paper do offer a degree of reassurance to investors, and address some of the concerns about how companies operate in other markets where dual class share structures are permitted without restrictions. In the event that these proposals are progressed, we would urge that they are only with the proposed limitations in place – particularly the rule that would effectively introduce a 5 year sunset clause on new listings *(Q20)*. We would be extremely concerned about any further reduction in standards beyond this.

However, we would ask that consideration is given to a weighted voting ratio of 10:1 on DCSS, rather than 20:1. Though we agree that the circumstances in which weighted shares can be used is limited, we believe that any move away from the basic principle of 'one share, one vote' should be as restrictive as possible. Combined with the proposed market capitalization rules, the proposals would enable some shareholders the ability to veto resolutions with less than 5% of the total shareholding – we would argue that in those circumstances those shareholders are not sufficiently invested in the company to justify retaining such authority. We believe that a more limited weighting rule would achieve the policy intent, whilst still prioritizing the rights of shareholders generally.

Free float requirements

For many of the reasons set out above, we remain opposed to any move away from the current rule on free float for premium listings, which is set at 25% *(Q25)*.

With regards to corporate governance, we believe that full consideration ought to be given not just to the possibility of a breach of free float rules resulting in suspension, but to the ability of minority investor groups to influence the long term direction of the company in relation to key long-term themes such as climate risk, diversity, and workforce factors – none of this appears to be reflected in the proposals. This is inconsistent with wider policy aims set out by Regulator bodies to improve diversity and inclusion in regulated firms.[7]

The current free float rule does not enable minority shareholders a veto but it does provide a tool for boards to be held to account. The UK's Corporate Governance Code requires that, when 20% or more of votes cast against a board's recommendation for a resolution, the company ought to explain what action it will be taking to consult and better understand the reasons for the dissent[8]. In such circumstances, the company is also listed on the Investment Association Public Register[9], which tracks and monitors significant dissent. In recent years, the increased scrutiny of these trends – particularly in relation to executive pay – has seen an increase in companies taking steps

[7] https://www.bankofengland.co.uk/news/2021/july/fca-pra-and-boe-set-out-plan-to-improve-diversity-and-inclusion-in-regulated-firms
[8] https://www.frc.org.uk/directors/corporate-governance-and-stewardship/uk-corporate-governance-code
[9] https://www.theia.org/public-register

to acknowledge shareholder concerns, with over 80% now making a public statement setting out how they plan to engage with stakeholders[10].

We believe that, without giving minority shareholders a veto on resolutions, these tools act as a positive force in the effective scrutiny of companies at a time of unprecedented interest in ESG factors. In recent years there has been a notable increase in shareholder activism in relation to climate change, and we are increasingly seeing shareholders use their vote as a tool[11]. We believe that the FCA's proposals will significantly weaken these features, and therefore further restrict the abilities of pension schemes to positively influence investee companies both in the long-term interests of pension savers, and in order to meet their own regulatory requirements.

We hope that these comments will be taken into account in the future consideration of these proposals. We would of course be happy to discuss this in more detail.

Yours sincerely,

Karen Hurst
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[10] https://www.theia.org/media/press-releases/shareholder-dissent-hits-quarter-ftse-all-share-companies-2019
[11] https://www.unpri.org/pri-blog/agm-season-2021-an-analysis-of-trends/8077.article