Proposed Rules May Attract More Companies With Dual-Class Share Structures to London Stock Exchange

Skadden

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If you have any questions regarding the matters discussed in this memorandum, please contact the following attorneys or call your regular Skadden contact.

Simon Toms
Partner / London
44.20.7519.7085
simon.toms@skadden.com

Danny Tricot
Partner / London
44.20.7519.7071
danny.tricot@skadden.com

Kathryn Gamble
Associate / London
44.20.7519.7219
kathryn.gamble@skadden.com

One Manhattan West
New York, NY 10001
212.735.3000

40 Bank Street, Canary Wharf
London, E14 5DS, UK
44.20.7519.7000

London's recent notable technology IPOs prove that European markets offer tech companies opportunities to achieve multibillion-dollar valuations and to meet their founders' requirements. In an attempt to increase the number of global IPOs in the U.K., in July 2021 the Financial Conduct Authority (FCA) published a consultation paper on the effectiveness of primary markets and proposals for significant changes to the U.K.'s listing regime, designed to give issuers greater flexibility while maintaining protections for investors.

Recent Tech IPOs

The following listings anticipated many of the themes in the FCA's consultation paper, including the increasing trend of dual-class share structures to allow founders to maintain some degree of control during an initial period post listing.

- **Wise** (July 2021 IPO) is the largest technology company to float and the first to do a direct listing on the London Stock Exchange. Wise's dual-class share structure granted enhanced voting rights to existing shareholders by means of Class B shares, enabling early investors to retain influence over the company's direction for an agreed period after listing. Skadden represented a significant shareholder in the transaction.
- **Deliveroo** (March 2021 IPO) adopted a dual-class share structure allowing the founder to be issued Class B shares that rank *pari passu* with the company's Class A shares. This guaranteed the founder's effective control for the three years following Deliveroo's listing by entrenching his board seat and enabling him to block a change of control. While the founder holds the shares, each will carry 20 votes on a resolution (compared to one vote per Class A share). The founder therefore held at admission 57.5% of the voting rights in Deliveroo and is able to block any ordinary or special resolution proposed at shareholder meetings.
- **The Hut Group** (THG) (September 2020 IPO) was the largest IPO in the U.K. since 2015, raising £1.88 billion. Under THG's dual-class share structure, the founder received a single "golden share" enabling him to maintain control, something previously not seen in European listings. The golden share does not entitle the founder to receive dividends or distributions and carries no voting rights, but does entitle him to the number of votes necessary to pass or defeat a change of control resolution for the three years following THG's listing.

FCA Consultation Paper

A short summary of some of the key changes proposed in the FCA's "Primary Markets Effectiveness Review" are set forth below. The FCA closed the consultation on September 24, 2021, and intends to implement technical changes before year end to assist companies considering funding rounds in the first quarter of 2022.

Remove the Distinction Between Premium and Standard Listings

In the U.K., a company can list on the Official List of the London Stock Exchange on either the premium segment or standard segment. While a premium listing is regarded as more attractive, a company with a dual-class share structure is not eligible for this option, and can therefore only be admitted to the Main Market through a standard listing.

The consultation considers whether to remove the distinction between premium and standard listings, thereby enabling companies with dual-class share structures to trade on a single Main Market. This development is likely to be welcomed by companies seeking to take advantage of the dual-class structure.

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Reduce Free Float to 10%

Currently, an issuer must demonstrate that at least 25% of its shares are "in public hands." Shares are only considered to be in public hands if, among other things, they are held by shareholders that each own less than 5% of the company's total shares. Some companies struggle to meet this requirement, limiting IPOs.

Lowering the minimum "free float" from 25% to 10% would enable more listings to satisfy the requirement, including more direct listings. This would be especially interesting to technology companies, which often have a significant number of minority shareholders that each hold more than 5% of the company's share capital, received in series financings during pre-IPO funding rounds.

Introduce an Exception for Dual-Class Share Structures

Dual-class share structures are of particular interest to founder-led companies, often found in the tech sector, by enabling founders to retain certain control rights while opening the company to public investment. However, the FCA and the U.K. market more generally continue to consider the best model of dual-class share structure, *e.g.*, a "golden share" structure or a Class A and Class B share structure.

The FCA proposes allowing companies with a specific form of dual-class share structure to be eligible for the premium listing segment. Five years after the listing, the weighted voting rights would need to be removed or the company would need to move to the standard listing segment or cancel its listing. Alternatively, the FCA proposes that the "enhanced rights" shares could automatically convert to ordinary shares upon transfer to a non-founder shareholder, as in the Deliveroo IPO, or that the shares could be cancelled, as in the Wise IPO. The duration and preferred structure will no doubt be the subject of continued debate, but we can expect dual-class share structures to become a much more common feature of newly listed London companies in the future.

The Impact of the FCA Proposals

The proposals are likely to bring the U.K. closer in line with other major global listing venues that have permitted dual-class share structures for some time. This would increase the attractiveness of the London Stock Exchange for companies with profiles similar to Wise, Deliveroo and THG, which have been required to list on the standard segment of the London market as a result of their dual-class share structures. Similarly, the reduction of the free float requirement may attract to the London Stock Exchange companies that do not need or wish to sell a large number of shares at IPO. The extent to which the proposals in the FCA's consultation paper are accepted, and their impact on the London market, will be seen in the coming months.