RESPONSE TO CONSULTATION PAPER

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By sending a response, you are deemed to have consented to the collection, use and disclosure of personal data that is provided to us for the purpose of this consultation paper or other policy or rule proposals.

Consultation topic:	**Proposed Listing Framework for Dual Class Share Structures**
Date:	27 April 2018
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Statement of interest (if applicable)	
Confidentiality	
I do not wish to be specifically identified as a respondent. ☐ **Please tick only if you do not wish to be specifically identified as a respondent.*	

General comment:

Before setting out our position on your consultation, we would like to highlight that CFA Institute and CFA Singapore remain steadfast in the belief that "one share, one vote" is the bedrock of good corporate governance standards. It is of our view that unequal voting rights would weaken the checks and balances between shareholders and management, and immunize management against stakeholders' critics and accountability.

In the probable case where companies with dual class share structures are introduced to Singapore, proper safeguards must be in place to protect shareholders from self-dealing and other misuses of corporate resources by company insiders for personal gain, or other actors not in the best interests of shareholders as a whole. Other safeguards should also be in place to mitigate risks of weakening corporate governance.

Question 1. Definition

SGX proposes to introduce the following new definitions:

(a) "dual class share structure" ("DCS structure") which refers to a share structure that gives certain shareholders voting rights disproportionate to their shareholding. Shares in one class carry one vote, while shares in another class carry multiple votes;

(b) "enhanced voting process" which refers to a voting process in a general meeting of the issuer where votes are cast on the basis that one MV share is limited to one vote;

(c) "multiple voting share" ("MV share") which refers to a share in a dual class share structure that carries multiple votes with the rights attaching to it specified in the Articles of Association or other constituent documents of the issuer in compliance with Rule 210(10) of the Mainboard Rules. Such share is neither listed nor traded. For the avoidance of doubt, save for multiple voting rights, the rights attaching to each MV share must be the same as the rights attaching to each OV share; and

(d) "ordinary voting share" ("OV share") which refers to a share in a dual class share structure that carries one vote with the rights attaching to it specified in the Articles of Association or other constituent documents of the issuer.

Do you agree with the abovementioned definitions?

Feedback:

No comment.

Question 2. Suitability requirement

The issuer and the issue manager must establish that the issuer is suitable for listing with a DCS structure. The factors that SGX may take into account include:

(a) the business model of the company, for example, that the company has a conceptualised long-term plan that contemplates ramping up growth at a fast pace;

(b) operating track record of the company or business;

(c) the role and contribution of intended MV shareholders to the success of the company or business;

(d) how actively involved the intended MV shareholders are in the company or the business;

(e) participation by sophisticated investors; and

(f) other features of the company or business that require a DCS structure.

Do you agree with the requirement that the issuer must establish that it is suitable for listings with a DCS structure? If so, please provide your views on the suitability factors that SGX should consider and reasons for your views.

Feedback:

We generally agree issuers should establish that they are suitable for listings with DCS structures, although we do find some of the considerations of suitability for listing ambiguous and subjective. For instance, although the participation of sophisticated investors as stated in (e) might suggest that certain degree of due diligence has been undertaken in some cases, these investors could also be only interested in the potential profits from investing in relevant companies. In the case of the latter, such provisions may not hold any substance.

We recommend SGX to publish the reasons for its assessment that a particular listing is suitable for a DCS structure as we believe there is significant investor interest on this subject.

Question 3. Moratorium

Do you agree that the holders of MV shares must observe a moratorium on the transfer or disposal of their entire shareholdings in the issuer in respect of their interests in both MV shares and OV shares for at least 12 months after listing?

Feedback:

According to the Mainboard Rules, depending on the profitability, market capitalization, and percentage of shareholding, the minimum period of moratorium is set between six to 12 months, while certain percentage of shareholding is subject to a different period of moratorium.

However, given the fact that DCS is a new shareholding structure introduced to the market and that it also involves a higher degree of complexity, we believe a general a moratorium on the transfer or disposal of their **all or part of** the shareholdings in the issuer in respect of their interests in both MV shares and OV shares for **at least 12 months** after listing appropriate.

In any event, any sale of MV shares should mean a reversion to "one-share, one-vote", as elaborated in Section III.4.3(a) of the consultation, without any exception.

Question 4. Maximum voting differential

(a) Do you agree that the voting rights attaching to MV shares should be capped at 10 votes per share?

Feedback:

We appreciate SGX's attempt to set limitations on the maximum voting differentials, which could be considered as a measure to reduce entrenchment issues and is a common practice in some European markets. However, we **strongly disagree with the proposed 10-to-1 maximum voting differential**.

According to the Global Governance Principles of International Corporate Governance Network (ICGN), the misalignment of economic interests and voting rights could result in managerial entrenchment. Similarly, the Organisation for Economic Co-operation and Development also suggests that a higher degree of economic involvement by management could lead to lower transaction costs and discourage opportunistic behaviours.

As requirements are currently laid out in the proposal, a shareholder with 9.1% economic stake in a company would possess over 50% of the voting rights. Under such arrangements, management would have more incentives and opportunity to

act for personal benefits than on behalf of other stakeholders. Such a lax corporate governance structure may lead to or induce management entrenchment.

Therefore, lowering the ratio to 3:1 would be more effective in holding the company management properly accountable for their actions, as they would need to have higher economic stake in the companies), thereby mitigating expropriation and entrenchment risks.

(b) Do you agree that the issuer should not be allowed to change the ratio post-listing?

Feedback:

We agree that, at the post-listing stage, the issuer should not be allowed to revise the ratio **in favour of the founder or other MV shareholders**.

However, in the case that the issuer considers it appropriate for the **vote-entitlement of MVs to rescind or be adjusted to a level more favourable to the OV** (e.g. voting differentials to be reduced from 5:1 to 3:1, or from 3:1 to 2:1), **subject to the approval of shareholders and SGX, such an action may be permitted**. Similar treatment should be permitted if a company is to unify the share structure and go back to just having one class of shares.

Question 5. Rights of OV shareholders

(a) With regard to the total voting control that OV shareholders can collectively exercise, do you think that OV shareholders must hold: at least 10% the total voting rights of the issuer on a one-share-one-vote basis (Option 1); or at least 10% of the total voting rights of the issuer (Option 2)?

Feedback:

We believe Option 1, which would mean a lower threshold to call for a general meeting, may be considered.

Our view is that OV shareholders should be allowed to call for a general meeting if collectively they hold at least 10% of the total voting rights of the issuer on a "one-share, one-vote" basis (Option 1). This will reduce the hurdle for OV shareholders to hold management to account and is particularly important if the MV shareholders hold an outsized number of votes. Assuming a 10:1 maximum voting differential, MV shareholders holding 30% equity share capital are entitled to 81% of voting rights. Under Option 2, it will take almost half of all OV shareholders to join forces before a general meeting is possible. This provides a significant hurdle for OV shareholders if they want to call management to account, with heightened risks to entrenchment.

(b) Do you agree that OV shareholders holding at least 10% of the total voting rights on a one-share-one-vote basis must be able to convene a general meeting?

Feedback:

Consistent with the reasoning underlying our position with voting control above, we consider it appropriate to amend the rules such that "OV shareholders holding at least 10% of the total voting rights on a one-share-one-vote basis must be able to convene a general meeting".

Question 6. Restriction on issuance of MV shares post-listing

(a) Do you agree that an issuer shall not be allowed to issue MV shares post-listing except in the event of a rights issue? Should the exception be extended to bonus issue, scrip dividends and subdivision and consolidation of shares which do not raise new funds?

Feedback:

We consider it appropriate that a requirement is set out such that founders would need to possess meaningful economic stake in the issuer to own a majority of voting power.

If the purpose of having DCS structures was to allow **entrepreneurs/founders** to focus on delivering and executing long-term visions and strategies for the companies despite having a lower economic stake (i.e. skewed proportionality between ownership and control), **then the degree of superior voting power should be capped at the level that was permitted when the companies are listed**.

We also believe issuance of common shares with zero voting rights should not be allowed. In the case where investment demand for equities with no voting rights arises, the issuer should consider the issuance of preference shares carrying a fixed coupon rate as the optimal alternative.

In short, further dilution of OV shareholders' voting rights should be avoided. Therefore, issuers shall not be allowed to issue additional MV shares once they are listed, without any exception.

(b) Under Section 64A of the Companies Act, a public company with a DCS structure shall not undertake any issuance of MV shares unless it is approved by shareholders by a special resolution. Do you agree that the issuance of MV shares must be approved by a special resolution of shareholders at a general meeting?

Feedback:

Issuance of MV shares must be approved by a special resolution of shareholders at a general meeting **prior to the listing of the companies**. No additional issuance of MV shares should be allowed after a company is listed.

(c) In undertaking any corporate action (including a share buy-back), do you agree that the issuer must ensure that the proportion of the total voting rights of the MV shares as a class against those of the OV shares after the corporate action will not increase above that proportion existing prior to the corporate action?

Feedback:

We agree that the proportion of the total voting rights of the MV shares as a class against those of the OV shares after the corporate action cannot increase above that proportion existing prior to the corporate action.

Question 7. Automatic conversion of MV shares

(a) Do you agree that initial holders of MV shares must be directors of the issuer?

Feedback:

We believe that **all** holders of MV shares must be directors of the issuer at the time of the listing **and** continue to perform such duties for the issuer.

From an investor's point of view, under the DCS framework, MV shareholders are given super voting rights because of their contribution to the development of the respective companies as influential directors of the companies. Likewise, if they are no longer directors, they should not be entitled to the rights to make the call for those companies, as they would not have the same duty of care and influence over company operations.

To be clear, DCS is a structure introduced to put someone that can generate value for the company and its stakeholder at the wheel. To permit anyone to have control of the company when he is no longer a director or shareholder of the company is a violation of the spirit of why we make exception for DCS.

(b) An issuer with a DCS structure must have automatic conversion provisions in its Articles of Association or other constituent documents meeting the following criteria:

i. If the holder of MV shares sells or transfers part or all of any interest in respect of his MV shares (which, for the avoidance of doubt, would include the beneficial interest and voting rights of the MV shares) to any party (including other holders of MV shares), whether or not for value, such MV shares will be converted into OV shares on a one-for-one basis.

ii. If the holder of MV shares ceases to be a director (whether through death, incapacity, retirement, resignation or otherwise), his MV shares will be converted into OV shares on a one-for-one basis.

Do you agree with the abovementioned automatic conversion events? If your answer is no to any of the conversion events, please state the reasons.

Feedback:

Consistent with our answer to Question 7(a), we agree with the aforementioned automatic conversion events.

In addition, we urge SGX to consider mandating time-based sunset provisions, which will mean the automatic conversion of super voting rights to regular voting rights on a "one-share, one-vote" basis after an agreed period between management and investors.

As a safeguard against DCS structures, time-based sunset provisions limit preferential voting rights to a defined period, and, in turn, relieve minority stakeholders of permanent exposure to moral hazard. Our view is also in-line with Robert J. Jackson Jr., the new U.S. Securities and Exchange Commissioner (SEC) who proposed that companies and their management should not be given preferential voting rights in a perpetual manner in his recent address. CFA Institute considers a mandatory sunset provision that automatically converts super voting rights to regular voting rights in three, or at most five years, to be appropriate.

Referring to a SEC preliminary study that covers some 157 stocks that had been listed with DCS structures since early 2000s, Commissioner Jackson suggested that firms with perpetual DCS structures had been traded at a significant discount to those with time-based sunset provisions. Whatever advantages a founder or an entrepreneur might bring to a company in its early years post-IPO would fade over time. He added that firms that had given up their DCS share structures saw a significant boost in company valuations. These findings illustrate the need for such time-based sunset provisions.

Noting that DCS structures do not provide equitable treatment of investors, such sunset clauses have been adopted by reputable technology-related companies when they went public in recent years, such as Mulesoft (2017), Fitbit (2015), Yelp (2012), Workday (2012) and Groupon (2011). The silver lining in recent developments is that a small but growing number of dual-class companies are adopting time-based provisions.

Perpetuity or long-term entitlement of super voting rights must be avoided. On top of the set of event-based sunset provisions proposed by the SGX, we are of the view that time-based sunsets should also be considered.

Last in order but not of importance, we would like to see how SGX envisages breaches of these sunset provisions could be properly monitored and enforced. As a highly regarded exchange and regulator, we are confident that SGX does have proper plans in place, but, as DCS is new to most of the investors in Singapore and in the APAC region, we believe stakeholders would be interested in learning more about the procedures and measures to be in place, as well as the consequences of the breaches.

(c) Do you agree that the shareholders can waive the conversion through the Enhanced Voting Process on the basis that one MV share is limited to only one vote?

Feedback:

We strongly disagree granting anyone the ability to waive the automatic conversion provisions through the Enhanced Voting Process, as it would give rise to further erosion of corporate governance standards by allowing waiver to any safeguards.

It is important to recognize that providing individuals who have no directorate or managerial functions with super voting rights is against the reason why DCS would be granted in the first place. While DCS structures are introduced to provide entrepreneurs with control of their companies even though they may lack capital for business expansion, such preferential treatment is by no means perpetual and should expire when the founders/entrepreneurs' influence over the company fades.

(d) Do you agree that the relevant holder of the MV shares, and his associates, should be required to abstain from voting on the resolution?

Feedback:

As stated in our answer to Question 7(c), we oppose waivers to the automatic conversion as it could give rise to entrenchment issues led by non-executive managers.

Question 8. Independence element on board committees

Do you agree that the majority of the Audit Committee, Nominating Committee and Remuneration Committee, including the respective chairmen, must be independent?

Feedback:

We agree that the majority of the Audit Committee, Nominating Committee and Remuneration Committee, including the respective chairmen, must be independent.

Question 9. Reserved matters under the Enhanced Voting Process

Do you agree that the following matters should require shareholders' approval through the Enhanced Voting Process (i.e. each MV share is limited to one vote)?

(a) changes to the issuer's Articles of Association or other constituent documents;
(b) variation of rights attached to any class of shares;
(c) appointment and removal of independent directors;
(d) appointment and removal of auditors;
(e) winding up of the issuer; and
(f) delisting of the issuer.

You may also propose other matters that should be subject to the Enhanced Voting Process. Please state reasons for your proposal.

Feedback:

We agree that matters (a), (c), (d), (e) and (f) should require shareholders' approval through the Enhanced Voting Process.

As explained in our answers to Questions 4(b) and 7(c), **(b) variation of rights in favour of MV shareholders should not be permitted under any circumstances**.

In addition to the list above, we also consider it appropriate to expand it to **cover "interested party transactions", "major transactions", and "very substantial acquisitions"**. That is, these matters should be voted on a "one-share, one-vote" basis, where DCS beneficiaries will not be able to exercise super voting rights.

We take note of the fact that the SGX has informed the Securities Industry Council to consider the implications of a DCS structure in the context of a takeover under the Take-over Code. We remain hopeful that appropriate amendments to the Take-over Code can be announced and implemented by the time DCS structures are introduced to the market.

Question 10. Disclosure of rights of shareholders

Do you agree that an issuer with a DCS structure should disclose the following additional information?

(a) The issuer must disclose its DCS structure, holders of MV shares and their respective shareholding and voting percentage both at the point of listing and thereafter, on a continuing basis, in its annual report.

(b) The shareholders' circular must contain information on the voting rights of each class of shares.

(c) The issuer must, in its prospectus, disclose the risks of DCS structures, rationale for adoption of its DCS structure, matters subject to the Enhanced Voting Process including implications to holders of OV shares, and key provisions in the Articles of Association or other constituent documents relating to DCS structures in a prominent manner.

(d) The issuer must include a prominent statement on the cover page of its prospectus, and on a continuing basis, in its announcements (including financial statement announcements), circulars and annual reports, highlighting that the issuer is a company with a DCS structure.

You may also suggest other disclosure requirements and provide reasons for your suggestion.

Feedback:

We fully agree with the abovementioned disclosure.

In addition, we note that the regulations do not require shareholders with MV shares to report their engagement to all shareholders. The area of concern we have is that after listing and satisfying the listing requirements, the original holders of MV become sleeping directors and not accountable for their future actions. Second, there is a risk of related party transactions undertaken by MV shareholders which over time impact the value share of OV shareholders. We believe there needs to be a further requirement to ensure that on a regular basis MV shareholders disclose in the annual report their engagement with the company, participation in management, etc., as follows:

(e) The issuer must, in its annual report, disclose the need for continuation with the adopted DCS structure, the engagement of MV shareholders in management of the public company, remuneration paid to MV shareholders, gross value of related party transactions, if any, that MV shareholders may have with other related entities, attendance of MV shareholders in board committee meetings and any conflict of interest that MV shareholders may have with new ventures and activities engaged in post listing and/or disclosures made in the last annual report.