Centre for Banking & Finance Law
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The Future of a Dual-Class Shares Structure in Singapore

Roundtable Discussion Report

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The views expressed in this report reflect the author's personal opinions and do not necessarily reflect the policies or views of the conference organizers, presenters, and discussants, and the Centre for Banking & Finance Law.

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The Centre for Banking & Finance Law (CBFL) at the Faculty of Law, National University of Singapore, focuses broadly on legal and regulatory issues relating to banking and financial services. It aims to produce research and host events of scholarly value to academics as well as of policy relevance to the banking and financial services community. In particular, CBFL seeks to engage local and international bankers, lawyers, regulators and academics in regular exchanges of ideas and knowledge so as to contribute towards the development of law and regulation in this area, as well as to promote a robust and stable financial sector in Singapore, the region and globally.

Table of Contents

I. BACKGROUND ON DUAL CLASS SHARES STRUCTURES 2

II. DUAL-CLASS SHARE STRUCTURE LISTING IN THE SGX 4

A. INVESTOR PROTECTION 4

B. CORPORATE GOVERNANCE 5

C. CONTINUING ROLE OF SINGAPORE AS THE FINANCIAL HUB IN ASIA 6

D. NECESSARY SAFEGUARDS 6

III. CONCLUSION 7

In early 2016, the "one share, one vote" restriction in Section 64(1) of the Companies Act (Cap. 50) was removed as part of a law amending certain provisions of the said Act. The amendment also introduced a new provision allowing public companies (private companies were allowed in 2003) to have multiple class shares structures subject to certain conditions. These developments have opened the floodgates and triggered a discussion between the Monetary Authority of Singapore (MAS) and the Singapore Stock Exchange (SGX) whether to allow dual-class shares (DCS) listings in the latter. In its FY2016 Annual Report, the Listing Advisory Committee (LAC) announced that it has approved the listing of DCS in SGX.[1] The LAC is an independent committee set-up in 2015 to advise SGX on its listing policies. The specific listing rules will only be finalized after SGX finishes with its planned round of public consultations. As part of this ongoing discussion, SGX, in partnership with the Centre for Banking and Finance Law (CBFL) and the Centre for Law and Business (CLB) of the National University of Singapore (NUS), Faculty of Law organized a roundtable discussion last November 14, 2016 featuring a renowned panel of experts in law and business to talk about the issues surrounding a DCS structure in the Singaporean context.[2] The purpose of this document is not merely to provide a report of the issues raised during the said event and the discussions which followed them; it also aims to provide a brief background on dual-class shares (DCS) for readers who are not acquainted with this topic.

I. Background on dual-class shares structures

Prior to the amendment of Section 64 of the Companies Act (Cap. 50), a share of stock in a company had to have the equivalent to one vote. This means that all shareholders, whether they be the founders or ordinary ones, are only entitled to one vote per share of stock that they own. The economic benefits that a shareholder receives in the form of dividend payouts are also correlated to the number of shares he/she owns in a company. One vote per share balances equity power and voting power since the more shares a shareholder owns, the more power such person has when it comes to making general corporate decisions.[3] However, the shareholders, as owners of the company, do not run its day-to-day operations in most cases. This task is entrusted to agents commonly known as the 'management' instead. The shareholders maintain control of the company by approving the decisions of the management when necessary or overruling them when so empowered in case such decisions are not in line with the shareholders' best interests. Thus, a one-share, one-vote structure ensures that the interests of the owners of the company are protected.

In 2012, this rule in Singapore was tested when Manchester United wanted to list in the SGX with a DCS structure. The proposed initial public offering (IPO) featured two classes

[1] Listings Advisory Committee, *FY2016 Annual Report* 2<http://www.sgx.com/wps/wcm/connect/b9f773a8-d2b0-4920-8466-6bf021df5332/SGX+Listing+Advisory+Committee+Report+FY2016.pdf?MOD=AJPERES&CACHEID=b9f773a8-d2b0-4920-8466-6bf021df5332> accessed last 1 December 2016.

[2] The panel of experts were: Ang Hao Yao, Wan Wai Yee, Goh Eng Yeow, Lawrence Loh, Patrick Grove, and Stefanie Yuen Thio. The discussion was moderated by Professor Hans Tjio of the CBFL. For additional details about the event, please visit: http://law.nus.edu.sg/pdfs/cbfl/events/SGXRoundtableDiscussion2016.pdf

[3] Katie Bentel and Gabriel Walter, 'Dual Class Shares' (Comparative Corporate Governance and Financial Regulation, Select Seminar Papers from University of Pennsylvania Law School, 2016) 2

of shares: Class A shares which will be held by the insiders of the company and Class B shares where the holders will have limited or zero voting rights. This is basically what a DCS structure is: the separation of voting power from equity in order for the insiders to maintain control of the company but enabling them to access the capital markets at the same time.[4] The DCS structure also separates voting rights from the economic interests in a share of stock so that while a certain class of share cannot vote, it still receives dividend payouts from the company. In the end, SGX decided to uphold the one share, one vote principle so Manchester United ended up listing in the New York Stock Exchange (NYSE) instead.[5] In defending its decision, SGX raised issues of entrenchment of control and the difficulty of getting a fair valuation of the two classes of shares in a takeover situation.[6]

According to Bentel and Walter (2016), "dual class stocks were first utilized in media companies as a means to protect the journalistic integrity of the news."[7] As a reflection of this trend, the Companies Act (Cap. 50) allowed the DCS structure insofar as newspaper companies are concerned. Prior to the 2016 amendment, Section 64(1) of the Companies Act (Cap. 50) provided:

> "Notwithstanding any provision in this Act or in the memorandum or articles of a company to which this section applies, but subject to sections 76J and 180(1), each equity share issued by such a company after 29th December 1967 shall confer the right at a poll at any general meeting of the company to one vote, and to one vote only, in respect of each equity share ***unless it is a management share issued by a newspaper company under section 10 of the Newspaper and Printing Presses Act (cap 206).*** " (emphasis supplied)

In the United Kingdom (UK) however, the DCS structure was said to be introduced as a measure of protection against corporate hostile takeovers.[8] Nowadays, DCS listings have been enjoying a resurgence elsewhere among high-tech and social media companies like Google, Facebook, and Groupon. The primary reason used to justify the structure of these companies is the need for the insiders to implement the long-term goals of the company and the possible impediment that the short-termism most stockholders pose.[9] This structure is also defended on the principles of freedom to contract.[10]

In the parliamentary deliberations with respect to the introduction of DCS in Singapore, it was acknowledged that this has been a contentious issue in various jurisdictions. Mr. Ong Teng Koon of Sembawang notes that the said kind of shares exemplifies the third objective of the amendments to the Companies Act to "ensure that the governance structure

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[4] ibid.

[5] Daniel Stanton and Fiona Lau, 'Manchester United drops Asia IPO for U.S.' *Reuters* (US, 13 June 2012) http://www.reuters.com/article/us-singapore-us-ipo-manchester-united-if-idUSBRE85C0MO20120613 accessed last 5 December 2016.

[6] Goh Eng Yeow, '"Dual-class shares" may not be apt for S'pore investors' *The Straits Times* (Singapore, 15 October 2014) <http://business.asiaone.com/news/dual-class-shares-may-not-be-apt-spore-investors> accessed last 5 December 2016.;

[7] *Bentel and Walter* (n 2) 18.

[8] Julian Franks, Colin Mayer, and Stefano Rossi, 'Spending Less Time with the Family: The Decline of Family Ownership in the United Kingdom' in Randall K. Morck (ed) *A History of Corporate Governance Around the World* (University of Chicago Press 2005) 604.

[9] Olivia Wang, "The Dual Class" (2015) 2 Emory Corporate Governance and Accountability Review 64, 65.

[10] Douglas C. Ashton, "Revisiting Dual Class Stock" (1994) 68 St. John's Law Review 863, 920.

strikes the correct balance between flexibility and transparency."[11] Support was shown for such shares in order to "maintain the relevance of Singapore as a financial hub and to maintain its competitiveness and attractiveness relative to [its] competitors."[12] Despite the acknowledgements made, the Members of Parliament stressed the need to ensure that the investors are fully aware when buying into these classes of shares. Concerns were also raised with respect to the remedies available to shareholders should the insiders take the company in a totally different direction and what happens when the super majority shares are sold to the market.[13]

Under the new Section 64A of the Companies Act (Cap. 50), both public and private companies are allowed to issue shares of different classes such as those that confer special, limited or conditional voting rights or even no voting rights subject to certain conditions. The said section also guarantees that the issuance of multiple classes of shares shall not impair the rights of shareholders under Section 74 of the same law.

II. Dual-class share structure listing in the SGX

As simultaneously being a listed company, a market operator, and a regulator, the SGX is burdened with the difficult task of striking a delicate balance between opening itself to innovations whilst maintaining a credible market. It must also be realized that the introduction of a DCS structure does not only concern SGX. Interests of other market players such as issuers which might want to issue DCS and investors who might purchase such shares, among others, also have to be taken into account. The future of Singapore as a regional finance hub also has to be borne in mind, should DCS be adopted or not in this country.

The roundtable discussion held last November 14, 2016 is only the beginning of a long and arduous process of evaluating carefully two major questions: first, "Whether to allow DCS listings in Singapore or not?" and second, "What are the framework and safeguards which will have to be adopted along with the DCS?". Before these two questions can be answered, preliminary issues such as: 1) investor protection; 2) corporate governance; 3) continuing role of Singapore as the financial hub in Asia; and 4) necessary safeguards must first be tackled.

A. Investor Protection

Contrary to popular perception, the debate about introducing DCS in Singapore does not only revolve around the country's need to boost investments and attract more listings. The investors' point of view must also be examined. As the target consumers of this new product, measures must be taken to ensure that the investors know what exactly he/she is buying, starting from the structure and framework of the listing up to his rights and entitlements as a shareholder of a company with a DCS structure. It is argued that the introduction of DCS is good because it enhances the investor choice. However, this choice will only be meaningful if there is an informed choice. It is therefore important that at the outset,

[11] Companies (Amendment) Bill, Parliament No. 12, Session 12, Volume 92, Sitting No. 15, 8/10/2014, Second Reading Bills.
[12] ibid.
[13] ibid.

the shareholders understand that they will be deprived of the power to make certain decisions later on.

Whilst investor knowledge is an important consideration, it should be noted that the DCS is not novel in this landscape. Preference and non-voting shares already exist in Singapore so the investors are already familiar with shares which have different voting structures. It follows that there are already entrenched shareholders in the country. Also, even without the DCS, there is already a dichotomy which presently exists between the minority and majority shareholders. Because of these, it cannot be assumed that the country's investors are not sophisticated enough for this kind of product.

However, even if Singaporean investors are already familiar with DCS, it is not a guarantee that investors will subscribe to these shares. Since Singapore's population is aging, most of the investors would perhaps rather put their money in something safer than equities. As such, there may not be a demand for DCS shares even if there is a supply of such.

B. Corporate Governance

Does DCS lead to the better performance of companies? In general, the evidence is a bit mixed. According to the newest literature, DCS companies perform better if they are more transparent – that is, if they already have a good corporate governance foundation. To maintain a high standard of corporate governance, it was suggested that the appointment of independent directors be made mandatory. The voting process for independent directors should also be an occasion where all shares carry the same votes. Doing this is no guarantee that such directors will regularly raise issues like they are supposed to, however. Moreover, such a concept might not fully work in an Asian society considering that the practice of having independent directors started in the west. Things are different here – shareholders' power is commonly unexercised and there is always a controlling shareholder that the board listens to.

The problem of management changes was also raised. As the DCS deprives the shareholders of the power to overrule management decisions, what will be the minority shareholders' recourse if the management changes its composition or changes the course of the company's direction? Also, the DCS structure might be difficult to dismantle later on. Enforcement tools that minority shareholders could use to discipline the management or corporate insiders might be important in this instance. For example, the US has a strong class action suit tradition which serves as an important disciplining tool. However, such a system does not yet exist in Singapore. By all accounts, few thought it a good thing in any case.

Concerns have been raised with this lack of enforcement mechanisms because it presumably signals that Singaporeans have been too dependent on the State to protect them. Because of this sentiment, questions have been raised whether it is time to introduce more civil shareholder suits in this jurisdiction. The preliminary conclusion is such a remedy might not be necessarily beneficial for the shareholders in the long run. Instead, SIAS is exploring ways for even small shareholders to raise meaningful questions at Annual General Meetings (AGMs) and the ultimate sanction they have is still to vote with their feet and to sell their shares.

C. Continuing role of Singapore as the financial hub in Asia

It is undeniable than in its more than fifty (50) years of (young) existence, Singapore's achievements has been remarkable. It is now one of the major financial hubs in Asia. If Singapore aspires to become an international centre and financial hub, it cannot get away from technology and disruption. Claiming that retail investors are not sophisticated enough is not a good mentality because Singapore should not be a nanny state. Instead, it should do more to attract multinational corporations to raise capital here. If one looks at the current listings in the stock exchange, it has very few non-local major companies in its roster. In the present globalized world, capital is fluid and can easily move across borders. If the regulatory framework and capital structure of the SGX are not sophisticated enough, companies might opt to list somewhere else. Therefore, Singapore should be all about innovation. DCS is one example of this. Whilst innovations should start in the private sector, there should be regulatory innovation too. Moreover, such innovation should not only consist of best practices from other jurisdictions; Singapore should also consider crafting its own responses which are attuned to its specialized domestic needs.

Without DCS structures, is Singapore actually missing out on avenues for start-ups to emerge? Some think so. Start-ups are the seeds of the future. Thus, providing them with different means for raising capital should be prioritized. The lack of a DCS option might also be dissuading family businesses from raising money in the capital market. By not having DCS here, Singapore might therefore be squeezing out huge chunks of growth.

The development of Singapore's capital markets through the adoption of the DCS structure should not come without caveats. It was also suggested that only companies which have room for growth or improvement could avail themselves of DCS. Companies should also not be valued based on profit earnings but on their growth potential. Target companies for DCS then should be large tech companies, start-ups and family companies.

On the other side of the coin, it has been observed by that Singapore is not a growth-driven market; most of the listed companies in SGX are big and established companies. Doubts have been raised whether there is need for financial innovation in the first place because of this. In addition, the investor profile in this country is more conservative in nature. Innovation can also attract miscreant companies to list in this jurisdiction. Scandals have also occurred because an innovative financial product (eg derivatives) fell through the cracks. If there is another corporate scandal stemming from this, some are doubtful if Singapore can easily absorb this since it is still a small market. This being said, it was noted by others that there have been corporate scandals here even without the DCS. It was also stated that for some companies like small and medium enterprises (SMEs), the stock exchange might not be the best place to raise money.

D. Necessary safeguards

At the outset, the DCS structure as recommended by the LAC to the SGX was to be used sparingly and not as a default rule. Whilst concrete standards have yet to be finalised, it has been further suggested that DCS shall only be allowed under exceptional circumstances. A thorough evaluation of the growth potential of the company was also suggested to be

included in the listing process. Another option could be to tag the DCS as a specialized investment.

Sunset clauses could also be considered which would give companies enough time for incubation. Also, should insiders decide to sell their shares in the secondary market, such shares should automatically convert to ordinary ones. It should also be remembered that there are different methods that can be used to entrench rights. Singapore can decide whether to allow only limited entrenchment or a full one. There was also a suggestion to impose fiduciary duties on holders of the “super” shares.

The LAC had also proposed a few measures such as the distinctive identification of DCS, 10:1 ratio of votes (so that there can be no non-voting shares), no conversion to DCS for existing listed companies, loss of enhanced votes in case of change of management, reversion to one vote per share in conflicts of interest situations, and making it mandatory for DCS companies to comply with corporate governance requirements in place of the existing comply-or-explain regime for normal SGX listed companies.

III. Conclusion

Based on the arguments proffered in this roundtable discussion, the initial conclusion seems to be that DCS might be something worth trying as long as investors are fully aware what they are actually buying. Moreover, the amendments passed by Parliament allowing multiple classes of shares might be a signal that Singapore is open to exploring this type of structure. It was cogently pointed out that the responsibility for the change cannot be shifted to SGX as the Government had clearly changed the law in that regard. Whilst concerns were raised with respect to checks and balances, entrenchment, and expropriation, such risks must always be balanced with the opportunities that DCS could bring. Questions were also raised on the issue of trust such as whether management could be trusted to make credible commitments and whether the market can be trusted to decide for itself. The roundtable discussion ended without any clear answers and solutions to the questions and problems raised. However, three key takeaways from this event could govern future public consultations on this matter: (1) the safeguards, if implemented, would be unique since they are more comprehensive than elsewhere; (2) Investor awareness and education are crucial. Investors must be given the choice to invest in DCS shares but only during the IPO stage; and (3) Any DCS framework will be supplemented by the existing SGX one.