QUOTED COMPANIES ALLIANCE

Generating growth in quoted companies

Spring Budget 2024 – Proposals for reform

This paper puts forward several fast fixes that we believe should be included in the Spring Budget on 6 March 2024. These solutions could have an almost immediate impact on reinvigorating the UK's public equity markets by improving trading volumes, enhancing investor appetite, and boosting corporate confidence.

1. Individual Savings Accounts (ISAs)

Proposal

The Government should reform ISAs to increase their appeal to retail savers and provide vital capital to British businesses by:

a) Simplifying the range of ISA products available, principally by combining Cash ISAs with Stocks & Shares ISAs;
b) Making the ISA a BRISA, backing growing British businesses;
c) Increasing the annual BRISA allowance from £20,000 to £25,000.

Details and key benefits of the proposals

a) *Simplify the range of ISA products available, principally by combining Cash ISAs with Stocks & Shares ISAs;*

Fewer ISA products would make the savings regime less complicated for new investors. It would enable them to switch their money between cash and shares more simply, to take advantage of changing risk appetite - and changing interest rates. It may also encourage some of the £285bn currently held in Cash ISAs to be redeployed more productively into UK shares.

b) *Make the ISA a BRISA, backing growing British businesses*

Restore the social contract between generous tax breaks and backing British businesses that was first introduced with Personal Equity Plans in 1986. From April 2024, impose a 50% minimal threshold so that for every pound invested in shares in overseas companies via a BRISA, at least one pound is invested in UK stocks too.

This measure would help to:

- Reconnect UK investors with the companies operating locally to them;
- Encourage a share-owning culture that benefits the UK economy;
- Replicate nationality-based conditions imposed in several other markets; and
- Enable savers to maintain a broad choice over where their investment is deployed.

c) *Increase the annual BRISA allowance from £20,000 to £25,000.*

The current ISA allowance has been unchanged for six years and inflation has eaten away at its headline value in real terms. Although the number of Stocks & Shares ISA investors who routinely use their full allowance is a minority (802,000 in March 2022[1]), raising the annual limit to £25,000 encourage equities advocates and an incremental £5,000 from each of them would add up to a meaningful amount flowing into UK stocks.

[1] New Financial, November 2023, A £10bn shot in the arm for UK equity markets: How ISAs could help kickstart a recovery in UK capital markets.

2. Stamp duty

The proposal

The Government should seek to scrap stamp duty on share trading for companies outside the FTSE 100 to help boost investment into these businesses. This can be done by extending the growth market exemption that currently applies to AIM companies to all businesses on the London Stock Exchange's (LSE's) Main Market that sit outside the FTSE 100.

Companies who sit within the FTSE 100 would continue to pay stamp tax on shares at the current rate of 0.5%. The majority of transactions that take place occur within these companies, as at the end of December 2023, the FTSE 100 had a net market capitalisation of over £1.9 trillion, with the FTSE All-Share Index having a net market capitalisation of £2.3 trillion[2]. It is expected therefore that the cost to the Treasury will not be substantial (see section below for further detail on estimated costs).

Careful consideration will have to be given to companies on the border of the FTSE 100 Index and qualifying and ceasing to qualify for the exemption. A company could become eligible or ineligible one calendar year after the end of the relevant financial year in which the company falls outside of, or enters into, the FTSE 100, respectively.

However, if this, or other ideas, regarding eligibility for FTSE 100 companies are considered to be too complicated, an alternative metric to use would be a market capitalisation threshold.

Key benefits of the proposal

- *International competitiveness*

The UK currently imposes a quadruple taxation on equities: dividend taxation, capital gains tax, income tax and a transaction tax via stamp duty (of which the UK has the highest rate in Europe).

This initiative would go some way to restoring the UK's competitive advantage versus many overseas listings venues. For instance, a similar exemption for smaller companies exists in Spain (for companies with a market capitalisation below €1 billion). The US and Germany currently have no stamp tax on shares and in France the rate is 0.1%. This would help to decrease the competitive disadvantage the UK has over other jurisdictions and direct capital into smaller, high-growth companies.

- *Stimulating investment into smaller company stocks*

There is often the perception that companies operating on the Main Market of the LSE are larger and more established than those on AIM. While this is correct at the top end of the market, many of the companies on the Main Market of the LSE are similar in size, with 366 of the 1,057 companies on the market having a market capitalisation of less than £100 million[3]. Moreover, over 730 companies on the market have a market capitalisation of less than £1 billion[4], which by most definitions, is considered to be small and mid-cap.

[2] Source: LSEG website, FTSE UK Index Series, FTSE 100 Index (Factsheet).
[3] Source: LSE website, News and Prices, Reports, as of end of December 2023.
[4] Ibid.

This proposal would therefore stimulate investment into smaller companies on this market, who may struggle to attract the levels of institutional investment that larger companies can. This will help to improve trading volumes and thus liquidity in these stocks, as it has for AIM companies.

- *Encouraging retail investment*

The current 0.5% charge on all transactions adds up for retail investors over time and is a barrier to investors investing in equity who can opt for alternative investments, such as a bond or a unit trust. Removing the charge would encourage more retail investors to invest in equities.

Data and estimated costings

According to some estimates, the initial loss of tax revenue to the Exchequer of scrapping stamp duty to all companies outside the FTSE 100 would amount to no more than £650 million annually[5].

Stamp duty is based on the value of shares traded, and as already highlighted, this means that the amount of stamp duty collected will be highly concentrated within the largest companies. We have provided estimates below on the level of stamp duty contribution for the different index categories[6].

Index	Contribution
FTSE 100	82%
FTSE 250	17%
FTSE Small-Cap and FTSE Fledgling	0.3%

Whilst the £650 million figure might seem significant, it is highly likely that, over time, the removal of stamp duty for these companies would result in more vibrant equity markets for smaller companies and increase tax revenue in the longer-term. Therefore, we expect that, due to greater levels of investment and growth, the initial reduction in tax will be fully offset.

However, and whilst we strongly believe this is the best approach, if this seems unpalatable, the Government could consider exempting all FTSE Small-Cap and FTSE Fledgling companies from stamp duty, which would cost an estimated £10 million, whilst also reducing the level of stamp duty for companies in the FTSE 250 to 0.2%.

Finally, we have provided estimates for the split of trading by market capitalisation, which gives an indication of the level of contribution to the share of stamp taxes that each market capitalisation band would pay[7]. A market capitalisation exemption could also be considered if the FTSE 100 metric is not deemed appropriate.

Market capitalisation band	Percentage contribution
<£1 billion	6.8%
£1-2 billion	7%
>£2 billion	86.3%

[5] Peel Hunt, August 2023, Thematic Research: Reinvigorating the UK Equity Market.
[6] Ibid.
[7] Hardman & Co/QCA research.

3. Investment vehicles

The proposal

The Government should seek to build on the investment incentives that work. To do this, we propose a two-fold approach:

a) Amending the Enterprise Investment Scheme (EIS) and Venture Capital Trusts (VCTs); and
b) The introduction of a new "UK Growth Trust", with wider eligibility than existing EIS and VCTs.

Amending the EIS and VCT schemes

The extension of the sunset clauses for the EIS and VCT schemes announced at the Autumn Statement in November 2023 were highly welcomed. However, we believe the Government should go further and give due consideration to the following:

- Amending the 7-year rule to allow tax breaks for acquisition financing and to determine a company's maturity through alternative metrics; and
- Streamlining the processing and eligibility criteria (particularly due to current delays and HMRC's new approach to eligibility).

The introduction of a new "UK Growth Trust"

We propose that the Government introduces a new "UK Growth Trust" in order to address the funding gap of scale-up stocks. This "UK Growth Trust" would have wider eligibility requirements than the current EIS and VCT schemes and be applicable to companies with a market capitalisation of less than £200 million. We believe that the Government should consult with industry stakeholders and market practitioners on what the eligibility requirements should be.

The Trust would then provide income tax relief for investors at a lower rate than the current schemes, such as, for instance, a rate of 15%.

Key benefits of the proposals

a) Amending the EIS and VCT schemes

The VCT and EIS tax reliefs are two vital risk capital schemes that are designed to help small and mid-sized companies attract investment. The schemes are critical to maintaining investment in early-stage companies, allowing these businesses to grow and plan for the future. The decision to extend the sunset clauses has helped to end the lack of certainty around their renewal which could have damaged confidence in investing in the UK's small businesses.

However, the Government should go further and seek to amend the eligibility requirements for the schemes, which, in their current form, are currently unnecessarily prohibitive and cause lengthy delays. Amending the eligibility requirements for the scheme and streamlining the processing system could result in a marked increase in the ability of some of the UK's smallest quoted companies to raise capital.

b) The introduction of a new "UK Growth Trust"

Currently there exists a significant funding gap for those outside the realms of EIS/VCTs. Once a company exceeds the thresholds making them ineligible for EIS/VCT investments, the company will likely find itself unable to attract investment because they are still too small and too high risk. There is evidence of companies increasing their market capitalisation and displaying impressive share price performance as a result of EIS/VCT and then being unable to locate investment once outside of the eligibility criteria. Ineligible companies will often find that they need more scale to find investors but cannot scale without significant investments from institutions that would have been provided by EIS/VCT. We believe that this occurs predominantly for companies within a market capitalisation range of between £15 million and £200 million.

The new "UK Growth Trust" would help to ameliorate these issues and provide vital funding for scale-up stocks. It would give industry impetus to target investment into this segment of the market and create a new sector of small-cap-focussed funds to allow easier access for different types of investors.

4. Equity research

Proposal

The Government should fast-track the introduction of the Research Platform, as proposed in Rachel Kent's Investment Research Review. This platform will "provide a central facility for the promotion, sourcing and dissemination of research on publicly traded companies – potentially open to all, but in particular, for smaller cap companies"[8].

The Research Platform could be supported by existing infrastructure providers in this area, including, for instance, the London Stock Exchange and the Aquis Stock Exchange, along with the main research houses/providers.

Finally, the Investment Research Review also recommended the implementation of a code of conduct for issuer-sponsored research. We have held conversations with Rachel Kent on this already and we would like to volunteer to devise and operate the proposed code of conduct. We would be able to gather the input of research houses/providers and other market participants through our extensive network in the public market space.

Key benefits of the proposals

The lack of equity research in the UK has primarily been the result of two factors: issues with commission (making it less appetising to produce research) and the introduction of MiFID II. We believe the Research Platform would reverse many of the current issues and revitalise investment research in the UK.

Similar arrangements to a Research Platform either exist, or have existed, in other jurisdictions, such as in France, Germany, Spain, Switzerland, Australia, Israel, Singapore and Malaysia, with the majority of these arrangements being focussed on small and mid-cap entities. Through allowing the research to be made publicly available – including to retail investors – the arrangements have helped companies to raise their profile amongst the investment community.

Proving the direct success of these arrangements is difficult, but there is evidence of improved share price performance and liquidity. More research, of a high standard and with a greater audience, will support long-term investment, resulting in better valuations for small and mid-caps and improvements to liquidity and ultimately growth.

Data and estimated costings

It is estimated that, at a minimum, the Research Platform would cost £100 million. It is imperative that this cost does not fall on companies, given the costs and burdens these companies are already facing. One potential mechanism to consider could be an levy on trading that is applied to investors.

[8] Rachel Kent, July 2023, UK Investment Research Review