Summary of Views in Submissions on the GEM Discussion Paper

HKEx published a Discussion Paper on the Growth Enterprise Market (GEM Discussion Paper) for public comment on 20 January this year. The paper discussed various issues concerning GEM and raised 12 questions for comment on the following three major areas:

- Need for and nature of a growth company market
- Possible structural options
- Other issues

At the close of the exposure period, which was extended one month to 31 May 2006, there were 16 submissions. Of these, three were from listed companies (including a listed company organisation), seven from market practitioners (four from securities professionals, one from accountants and two from lawyers), four from other organisations and two from other individuals.

The full text of the individual submissions is available on the HKEx website (http://www.hkex.com.hk/consul/response/GEMdp-r.htm).

Respondents' views on the 12 questions raised in the GEM Discussion Paper are summarised below.

In the main, among the submissions which expressed opinions on the respective subjects, support was shown for the following:

- ***Having a growth company market in Hong Kong.***
- ***Opening the market to companies from all jurisdictions and at all stages of development, and to all investor groups.***
- ***Establishing a new alternative market with a lighter touch or a disclosure-based buyer-beware regulatory regime.***
- ***Having a flexible, streamlined listing process with low-cost access to capital.***
- ***Establishing a life-long nomad-type* sponsor regime or enhancing the sponsor role.***
- ***Introducing market making or a liquidity provider system.***

HKEx will take into account respondents' views in formulating its proposals on the further development of GEM and related matters. HKEx is mindful of the position of existing GEM-listed companies and will consider their interests carefully when formulating its proposals. Such proposals will be subject to separate consultation.

NEED FOR AND NATURE OF A GROWTH COMPANY MARKET

Q1. Is there a need for a growth company market in Hong Kong?

Of the 16 submissions, 14 indicated that there is a need for a growth company market in Hong Kong. One replied in the negative and one did not give an indication.

Q2. If so, should the market primarily serve local Hong Kong companies, or should it target Mainland-based companies or regional/international companies?

Twelve submissions responded to the question. Eleven of them indicated that the market should serve companies from all jurisdictions; among them two pointed to Mainland China specifically. One suggested broadening the scope to include other Asia-Pacific countries with respectable regulatory frameworks.

Q3. At what stage of development should companies be admitted to the growth market – at start-up stage, or at a more mature stage?

Ten submissions responded to the question. Of these, five considered that companies at all stages of development should be admitted; four preferred more mature ones (no start-ups); and one organisation said that its members had diverse opinions. Three submissions asked for restrictions on "cash shells".

Q4. What should be the core investor group for the growth company market – retail, professional and/or institutional? Should the growth company market be restricted to professional and institutional investors only?

Eleven submissions responded to the question. Eight considered that the market should be open to all investor groups. One organisation said that its members had diverse opinions. Two felt that it should open to professional and institutional investors only.

Q5. Depending on your answers to the foregoing questions, what kind of regulatory regime would be appropriate for the growth company market? In particular, should growth companies have low-cost access to public capital, or should they, because of their higher risk, be required to comply with procedures that dictate relatively higher costs than those for Main Board companies?

Fourteen submissions responded to the question. Five asked for a disclosure-based "buyer-beware" and/or a lighter regime; another two asked for a lower cost regime. Two asked for a strengthened regime or a regime no less onerous than the Main Board. One asked for an acceptable, reasonable and practical regime. Two suggested a regime similar to, or adapted from, that of the Main Board. One indicated that the existing regime hampers flexibility. The remaining one pointed out that a lighter touch regime is preferred if the market is to be an alternative market. In addition, two asked for a delisting mechanism while one did not support it.

POSSIBLE STRUCTURAL OPTIONS

Q6. Bearing in mind your responses to questions 1 to 5 above, please comment on the suitability of the following possible structural options for a growth company market in Hong Kong:

(a) GEM as a second board
(b) GEM and the Main Board to merge as a single board:
- **i. Universal Single Board – GEM and the Main Board to merge as a single board with no distinction between them;**

ii. Tiered Single Board – GEM and the Main Board to merge as a single board with the growth market forming the lower tier and the existing Main Board the upper tier. Further tiers might be introduced as well.

(c) New alternative market – GEM to merge into the Main Board, and a new market with an enhanced regulatory regime is launched for growth companies.

(d) Others – do you have any other suggested structural options for GEM?

Of the 14 submissions which agreed to have a growth company market, 11 indicated their preferred option. Among them, seven preferred a new alternative market. Among the three which did not indicate their preferred option, one supported the AIM model in the UK as a long term goal. One explicitly objected to the new alternative market model and preferred GEM as a second board, with the universal single board as the second choice. Another one also supported the second board option. One supported an alternative board for companies not meeting Main Board requirements. One suggested over-the-counter (OTC) automated trading services to compete with HKEx's market.

Q7. Based on your preferred structural option for GEM, do you have any specific views or recommendations concerning:

(a) the targeted issuers (eg type of business, stage of development) and investors (eg retail, professional, institutional)

(b) the regulatory approach,

(c) the initial listing requirements and the listing process,

(d) the process of ongoing regulatory supervision,

(e) the disclosure and corporate governance requirements, and

(f) the roles of sponsors and other professionals?

The questions on targeted issuers and investors and the regulatory approach have been addressed in Q2, Q4 and Q5 above.

Eight submissions responded to the question on initial listing requirements and listing process. Three asked for the initial listing requirements to be raised; one felt that the requirements need not differ substantially from the existing ones; one suggested no requirements in size and public float; and one suggested a tiered structure with a graduation system. Four asked for a flexible/streamlined listing process. One said that the lock-up period should remain at a maximum of 12 months.

Five submissions responded to the question on ongoing regulatory supervision. Two felt that that the professionals/sponsors should bear more responsibility, one of them asked for post-vetting. One considered that supervision should be no less onerous than for the Main Board. One indicated that it is so far so good. One asked for more effective regulation with stronger sanctions.

Seven submissions responded to the question on disclosure and corporate governance requirements. Three asked for a buyer-beware approach or more disclosure. Two considered that it should be no less onerous than for the Main Board or in line with the Main Board. One asked for more corporate governance requirements. One asked for disclosure and corporate governance to be flexible and appropriate.

Eleven submissions responded to the question on sponsor roles and six of them considered that they should be enhanced — including four asking for a life-long nomad-type sponsor regime. However, two indicated that Hong Kong is not ready for a life-long nomad-type model, and one of these asked for more regulatory focus on accountants. One indicated that sponsors should have reasonable skills and responsibilities. Two indicated that there should be safe harbour rules for sponsors who perform with due competence and in good faith.

Q8. If you consider that there is no need for a growth company board in Hong Kong, what should be done with GEM and its existing issuers?

Only one submission indicated that there is no need for a growth company board. It suggested transferring all GEM-listed companies to the Main Board and abolishing GEM.

Q9. What, if anything, should be done with delisted companies? Should there be a separate market for trading these companies?

Eight submissions responded to the question. Of them, five considered that no separate market should be provided; three asked for a trading facility, one of these suggesting an OTC market.

OTHER ISSUES

Q10. Do you have any suggestions on how to raise the profile of companies listed on the growth company board?

Ten submissions responded to the question. Five asked for more promotion. Three suggested raising the overall market profile — higher standards, liquidity and transparency, or a firm and clearer policy. Two suggested that a lightly regulated board would help. One responded that there is no such need.

Q11. Should more information be provided on growth companies? If so, what information, and who should provide it?

Seven submissions responded to the question. Two asked for half-yearly instead of quarterly reporting while one supported quarterly reporting. One asked for reporting to be in line with that of the Main Board. One asked for proper information but not more of it, while another one welcomed more information. One mentioned that prospectuses should be in clear, plain English and another two commented that prospectuses are too voluminous.

Q12. Should market making be permitted on the growth company board? If so, what should be the obligations of and incentives provided to market makers?

Eight submissions responded to the question, seven of them supported the provision of market making or a liquidity provider system while one was not sure of its necessity. One suggested obligations to be similar to those of warrant issuers. One suggested that the system be the same as on AIM. One suggested market makers be voluntary and independent of the issuers.

* Please see page 44 of the GEM Discussion Paper for information on nomads (nominated advisers).