

## **HKEX Consultation Paper on Overseas Issuers** **Comments provided by HKIFA members (May 31, 2021)**

### **Proposed Core Standards**

- We are in full support of the HKEX proposal to come up with a single common set of Core Standards; as the current framework is fragmented and disjointed. A common set of Standards can ensure consistency and clarity, provide a level playing field and prevent regulatory arbitrage.
- To be meaningful, the Core Standards should set a baseline that would ensure adequate safeguard of investor interests.
- However, we note that there are certain key gaps that need to be addressed before the proposed Standards can provide the necessary protection.
  - ✚ a key gap is that the Core Standards fall short in protecting minority shareholders regarding related party transactions (RPTs), which is a perennial problem in HK, given the prevalence of controlled companies. We strongly believe that there should be explicit provisions in the Standards which state that:
    - directors/controlling shareholders should abstain from voting on board resolution in which they or their close associates have a material interest.
    - the votes of interested parties must not be counted when approving RPTs, even if this might be allowed in their primary markets.
    - more generally, issuers will be required to meet the requirements (as covered in Chapter 14 (notifiable transactions) and Chapter 14A).
  - ✚ the threshold to requisition a meeting: this should be reduced from 10% to 5% of the voting rights.
  - ✚ variation of class rights/constitutional documents: the threshold of the definition of “super-majority vote should be aligned across the board – all issuers should adopt 75%. We see no compelling reasons why there should be differentiated treatments, by allowing some issuers to use a lower threshold of 66%.
  - ✚ that there should be explicit provisions requiring financially material ESG issues to be included as an integrated report in the same document as the standard Financial Statements. Investors strongly believe that all issuers should be required to meet HKEX’s CG and ESG requirements as a minimum.
- The Core Standards, once developed, should apply across the board, i.e. to applicants as well as existing listed issuers. We agree that to allow sufficient lead time, issuers, can until their second annual general meeting, make any necessary amendments to their constitutional documents to conform with the Core Standards.

### **Waiver applications**

As a general principle, we would emphasise the importance of having robust frameworks and controls around the use of any waivers. Any waivers should be fully disclosed to shareholders.

**Dual primary:**

- The proposal to codify certain Common Waivers and the prescribed conditions as described in paragraph 158 of the CP are helpful.
- As to whether:
  - ✚ Grandfathered Greater China Issuers and Non-Greater China Issuers with Non-compliant WVR and/or VIE Structures should be able to apply for dual primary listing directly on the HKEX as long as they can meet the relevant suitability and eligibility requirements under Chapter 19C of the Listing Rules for Qualifying Issuers with a WVR structure.
  - ✚ both types of issuers should be allowed to retain their Non-compliant WVR and/or VIE Structures (subsisting at the time of their dual primary listing in Hong Kong) even if, after their listing in Hong Kong, they are de-listed from the Qualifying HKEX on which they are primary listed.

One must be mindful that WVR and VIE structures should be looked at differently as the nature is different.

- ✚ For VIE Structures, in certain circumstances, this is probably the only viable route and thus there is a valid reason to retain this structure. However, as this structure is very much subject to policy and regulatory changes, we believe that it is important is that there are robust and timely disclosures about its structure and any changes.
- ✚ But we do not agree with allowing ‘non-compliant’ WVR structures to apply for primary listings while retaining the non-compliant WVR structures. By opening the door to WVR - starting from individuals and moving to corporates, the HKEX has already been allowing the encroachment of the interests of minority investors. This proposal goes even further by embracing issuers that do not meet the criteria. This in effect means that the HKEX is trying to mainstream the WVR structure, which fundamentally militates against investor interests.
- ✚ In general for WVR, we believe that there should be time-based sunset provisions; and renewals, if any, should be subject to minority shareholder approvals.

**Secondary listing:**

- We agree that the HKEX should apply the test for a reverse takeover, as described in paragraph 210 of the CP, if the HKEX suspects that an issuer’s secondary listing application is an attempt to avoid the Listing Rules that apply to primary listing.
- There should be provisions that give the HKEX the discretion to reject an application for secondary listing if it believes the listing constitutes an attempt to avoid the Listing Rules that apply to primary listing. But we hope there is more visibility re how this discretion is being exercised, if at all.
- Regarding the proposed codification of the principles set out in paragraph 215 of the CP on which exemptions/waivers are granted, we do not have issues. But the principles stated are only high-level ones that pertain more to the markets. We wish to have greater clarity as to the company-level criteria that the HKEX adopts when it reviews the applications.
- We agree that codifying the Automatic Waivers and conditional Common Waivers in the Listing Rules for all issuers with, or seeking, a secondary

listing, would be helpful as this gives the market greater clarity and certainty as to the requirements applicable to issuers.

- We agree with the removal of the current condition for granting a waiver from the shareholders' consent requirement relating to further issues of share capital for secondary listed issuers as described in paragraphs 218 and 219 of the Consultation Paper. The right of pre-emption is a fundamental ownership right for shareholders.
- We are in full support that secondary listed issuers should comply with the requirements for a diversity policy (not just on gender, but other aspects) and for such policy to be disclosed in their annual reports. They should disclose that policy, the metrics being used, and progress made against them in the Annual Report.

### **Trading migration requirement**

- We agree that the Trading Migration Requirement should cover all issuers with a secondary listing so as to remove inconsistencies.
- As a principle, we do not agree that companies that de-list from their qualifying exchange will be allowed to retain their WVR arrangements (therefore not complying with Chapter 8A).
- HKEX should consider requiring secondary listed issuers of significant market capitalization and trading volume in Hong Kong to become dual primary listed after a certain period of time, eg three years of their secondary listing, when they should then become subject to the standard listing requirements in HK as well as the listing requirements of their initial primary listing. Otherwise as secondary listings become a significantly growing segment of the market, it could potentially lead to a drop in the overall regulatory standards.

### **Consolidation of the requirements**

- We agree with the following proposals:
  - ✚ to codify requirements (with the amendments set out in the Consultation Paper) relating to secondary listings in Chapter 19C of the Listing Rules and re-purpose Chapter 19 of the Listing Rules as one dedicated to primary listings only would be helpful.
  - ✚ to adopt the quantitative eligibility criteria as proposed in paragraphs 199 and 201 of the CP to consolidate the various routes.
  - ✚ to exempt the following types of applicants from the listing compliance record requirement – those without a WVR structure that are well-established and have an expected market capitalisation at listing that is significantly larger than HK\$10 billion.
  - ✚ new secondary listing applicants without a WVR structure (including those that have a centre of gravity in Greater China) should not have to demonstrate to the HKEX that they are an “Innovative Company”.

### **Accounting/audit standards**

- We believe that:
  - ✚ using accounting standards different from IFRS should be acceptable provided that there is robust reconciliation for each line impacted of the

financial statements to ensure investors know the differences and can adjust.

- ✚ re the proposal that a dual primary or secondary listed issuer that adopts a body of alternative financial reporting standards for its financial statements (other than issuers incorporated in an EU member state which adopted EU-IFRS) must adopt HKFRS or IFRS if it de-lists from the jurisdiction of the alternative standards – there shouldn't be a need to have such a switch if the company will reconcile its financial statements under alternative financial reporting standards to HKFRS or IFRS.
- ✚ helpful to have disaggregated disclosure by line of the financial statements reconciling the accounts under US GAAP to under IFRS or HKFRS.
- We generally agree the Listing Rules should retain as guidance:
  - ✚ the alternative auditing standards listed in paragraph 249 of the CP that can be used to audit the financial statements of Overseas Issuers. The 7 sets of alternative standards are acceptable, and comparable to that required by HKICPA or the IAASB.
  - ✚ the list of acceptable alternative financial reporting standards that can be used to prepare the financial statements of Overseas Issuers subject to the current limitations on their use as set out in Table 7 (Schedule E) These standards are understood by the market and appear reasonable.
- We agree an issuer which:
  - ✚ de-lists from a jurisdiction of an alternative financial reporting standard should: (a) be given an automatic grace period (i.e. an application to the HKEX is not required) within which to adopt IFRS or HKFRS; and (b) that this grace period should end on the issuer's first anniversary of its de-listing. The timeline is reasonable.
  - ✚ wishes to adopt US GAAP for the preparation of its annual financial statements must include a reconciliation statement showing the financial effect of any material differences between its financial statements and financial statements prepared using HKFRS or IFRS. Having a reconciliation allows for global peer comparisons and enhances transparency.

### **Company Information Sheet requirement/Guidance**

- We support clear and full disclosures re the items described in paragraphs 283 to 288 of the Consultation Paper. Shareholders should have the right to understand and easily locate information on the details of waivers and the differences between the overseas requirements to which an Overseas Issuer is subject and the Hong Kong requirements.
- The Company Information Sheet requirement should be applied not just to (a) secondary listed issuers; but to (b) any other overseas issuers. We don't see on what grounds would the publication of a Company Information Sheet be deemed as not useful to Hong Kong investors.
- We believe that amalgamating the guidance described in paragraphs 289 and 290 of the CP into one guidance letter for Overseas Issuers would be helpful.

(End)