Freshfields' response to HKEX Consultation Paper on Listing Regime for Specialist Technology Companies

Question 2:	**Do you agree with the list of Specialist Technology Industries and the respective acceptable sectors set out in paragraph 4 of the Draft Guidance Letter (Appendix V to the Consultation Paper)?** **Please give reasons for your views. If you answer is "No", please provide alternative suggestions.**
A:	We agree with the proposed non-exhaustive list of Specialist Technology Industries and the respective acceptable sectors set out in paragraph 4 of the Draft Guidance Letter (Appendix V to the Consultation Paper) as well as the proposal to update the list by way of a guidance letter to reflect the latest technology trends from time to time. While there is a mechanism and process to update the list, we suggest that the Exchange should consider including blockchain technology as an acceptable sector under the category "Next-generation information technology" in the initial non-exhaustive list. Blockchain technology is widely considered as a rapidly advancing next-generation technology that has the potential to bring revolutionary changes in a number of sectors, including banking and finance, currency, healthcare, property records, smart contracts and supply chain.
Question 8:	**Do you agree that a Commercial Company applicant must have a minimum expected market capitalisation of HK$8 billion at listing?** **Please give reasons for your views.**
A:	Market participants have indicated to us that the proposed threshold of HK$8 billion at listing is too high and there will be a very limited number of companies that can satisfy this requirement, especially in the current macroeconomic environment. This threshold is also significantly higher than the equivalent thresholds of the NYSE (HK$1.6 billion), NASDAQ (HK$1.2 billion), LSE (HK$296 million), SSE (Star Market) (HK$1.8 billion in normal circumstances) and SGX (HK$1.65 billion) as referred to on page 22 of the Consultation Paper. In addition, we believe that a high market capitalisation at listing does not always fairly reflect the listing applicant's quality and compliance standards. While we acknowledge that there is a need to set a minimum market capitalisation threshold, we are of the view that it is equally important that Hong Kong remains competitive by having a threshold that is comparable to other key competitor markets. Market participants have indicated to us an appropriate minimum market capitalisation threshold should be in the range of HK$4 billion to HK$6 billion.

Question 9:	**Do you agree that a Pre-Commercial Company applicant must have a minimum expected market capitalisation of HK$15 billion at listing?** **Please give reasons for your views.**
A:	Similarly, market participants have indicated to us that the proposed threshold of HK$15 billion at listing is too high and there will be a very limited number of companies that can satisfy this requirement, especially in the current macroeconomic environment. More importantly, the HK$15 billion threshold for a Pre-Commercial Company is almost double the HK$8 billion threshold for a Commercial Company. There is a real concern as to how a Pre-Commercial Company (without any revenue requirement) can justify a much higher market capitalisation than a Commercial Company. We would therefore suggest that the Exchange consider an appropriate lower threshold with a view to maintaining competitiveness vis-à-vis other key markets. Market participants have indicated to us that an appropriate minimum market capitalisation threshold should be HK$8 billion and the proposed threshold for a Pre-Commercial Company applicant should not be significantly higher than the proposed threshold for a Commercial Company applicant.
Question 12:	**Do you agree that (a) a Commercial Company must demonstrate year-on-year growth of revenue derived from the sales of Specialist Technology Product(s) throughout the track record period, with allowance for temporary declines in revenue due to economic, market or industry-wide conditions; and (b) the reasons for, and remedial steps taken (or to be taken) to address, any downward trend in a Commercial Company's annual revenue must be explained to the Exchange's satisfaction and disclosed in the Listing Document?** **Please give reasons for your views.**
A:	We are concerned that the proposed year-on-year revenue growth requirement for a Commercial Company (even with allowance for temporary declines) may have a significant impact on the attractiveness of the new listing regime and the number of potential listing applicants. This is amplified by the fact that there is no such requirement in the other key markets. We believe that the other safeguards such as the minimum revenue threshold for the most recent audited financial year, the minimum expected market capitalisation at listing and the detailed disclosure requirements around revenue in the Listing Document should be sufficiently robust to ensure that listing applicants are of an acceptable quality. Revenue growth during the track record period can be affected by many different factors, and in some cases can even go beyond economic, market or industry-wide conditions. For example, the sales of a Specialist Technology Product may be exceptionally high in year 1 but decline in year 2 only because year 1 was an exceptional year. The decline can also be attributable to factors such as the focus of the company's efforts and resources has shifted to the launch of a new Specialist Technology Product in year 2/3 which is

	potentially much more profitable, or increased competition from similar products in the market in year 2. These factors however do not necessarily mean that the Specialist Technology Product launched in year 1 is no longer good technology or that the sales of the Specialist Technology Product in year 1 will not increase in subsequent years. The market landscape often changes quickly in the technology world and certain players may be forced out of the market over time. We therefore suggest removing this year-on-year revenue growth requirement for a Commercial Company.
Question 15:	**Do you agree with the proposed method for determining the amount of qualifying R&D investment and the total operating expenditure as set out in paragraph 141 of the Consultation Paper?** **Please give reasons for your views.**
A:	We agree in principle with the proposed method for determining the amount of qualifying R&D investment and the total operating expenditure as set out in paragraph 141 of the Consultation Paper. However, it is not entirely clear to us whether interest expense and other costs to specifically finance R&D investment would qualify as R&D investment for the purposes of calculating the 15% (for Commercial Companies) and 50% (for Pre-Commercial Companies) thresholds. Accordingly, we suggest clarifying the above by way of a guidance letter as referred to in the proposed Rule 18C.04 of the Listing Rules.
Question 20:	**If your answer to Question 18 is "Yes", do you agree with the proposed definition of a sophisticated investor (including the definition of investment portfolio" as set out in paragraphs 159 to 162 of the Consultation Paper?** **Please give reasons for your views.**
A:	We agree that an applicant applying to list under the proposed regime should have received meaningful investment from Sophisticated Independent Investors (SIIs) as referred to in Question 18. However, in relation to the "sophisticated investor" examples set out in paragraph 160 of the Consultation Paper, we are of the view that the thresholds in (a) and (b) may have been set too high, especially in the current macroeconomic environment. Under the Guidance Letter on Special Purpose Acquisition Companies (***SPACs***) (*HKEX-GL113-22*), the "significant investors" referred to in Rule 18B.42 of the Listing Rules must either be: (a) an asset management firm with assets under management of at least HK$8 billion or (b) a fund with a fund size of at least HK$8 billion.

	Under the Guidance Letter on Suitability for Listing of Biotech Companies (*HKEX-GL92-18*), the Exchange stated the following as examples of a "Sophisticated Investor" for the purpose of applications for listing under Chapter 18A: (a) a dedicated healthcare or Biotech fund or an established fund with a division/department that specializes or focuses on investments in the biopharmaceutical sector; (b) a major pharmaceutical/healthcare company; (c) a venture capital fund of a major pharmaceutical/healthcare company; and (d) an investor, investment fund or financial institution with minimum AUM of HK$1 billion. The proposed thresholds of HK$15 billion set for an asset management firm, a fund and a company having a diverse investment portfolio are substantially higher than the equivalent thresholds applicable to SPACs and Biotech Companies. It is also our understanding that there are practical difficulties in finding an asset management fund or a fund that met the much lower HK$8 billion threshold in the case of SPACs. While it is proposed that the Exchange will assess whether an investor is a "sophisticated investor" on a case-by-case basis (by reference to its relevant investment experience, knowledge and expertise in the relevant field which could be demonstrated by its net assets, AUM, size of its investment portfolio or track record of investments, where applicable), we suggest that the Exchange consider revisiting the AUM and fund size thresholds for Specialist Technology Companies for the reasons set out above. Furthermore, it is not entirely clear about the cut-off time for each of these thresholds; for example, whether it should be referenced to the issuer's date of listing application or the end of the last financial year prior to the listing application. It would be helpful if the Exchange can give more guidance on this. Another suggestion is that we would encourage the Exchange to circulate draft FAQs on Specialist Technology Companies for comments from market participants in advance. This will help clarify some common questions that the market may have in the early stage. It can also significantly reduce the time for pre-consultation with the Exchange and align understanding across the market.
Question 24:	**Do you agree that a Pre-Commercial Company applicant must demonstrate to the Exchange, and disclose in its Listing Document, a credible path to the commercialisation of its Specialist Technology Products, appropriate to the relevant Specialist Technology Industry, that will result in it achieving the Commercialisation Revenue Threshold?** **Please give reasons for your views.**
A:	We agree but would suggest that the Exchange clarify the specific documents which would need to be submitted at the time of the A1 filing to show there is a credible path to the commercialisation of the Pre-Commercial Company's Specialist Technology Products. For example, it would be helpful to understand if the binding contracts or non-binding framework agreements referred to in paragraph

	176 of the Consultation Paper and/or any excel spreadsheet showing the projected financial performance associated with the Specialist Technology Products over the expected timeframe to achieve the Commercialisation Revenue Threshold are required to be submitted at the time of the A1 filing.
Question 37:	**Do you agree that a Specialist Technology Company applicant's Listing Document must include the additional information set out in paragraph 32 of the Draft Guidance Letter (Appendix V to the Consultation Paper) due to it being a Specialist Technology Company?** **Please give reasons for your views.**
A:	*General comment on qualitative disclosures* We note the Exchange's comment on pages 62 and 64 of the Consultation Paper that detailed qualitative disclosure should be provided describing a Specialist Technology Company's intellectual property and the protective measures it has taken to avoid infringement or duplication of its innovations. While we agree in principle that qualitative disclosures offer a more reliable basis on which to make an investment decision than a list of rights or the inclusion of technical details that are unlikely to be comprehensible to, in particular, a retail investor, providing a meaningful assessment of a listing applicant's intellectual property position will require a detailed understanding of intellectual property and how intellectual property maps onto the technical features of products, process methods and other technologies. In this regard, listing applicants may need to engage intellectual property experts to conduct due diligence on the Specialist Technology Product(s) and issue opinions to support the qualitative disclosures. The Exchange should clarify in its guidance letter if it expects an expert opinion to be provided to support the assessment of the listing applicant's intellectual property. *Highlight any risk of intellectual property infringements in the Summary and Risk Factors sections and include a positive statement by the directors* We note the proposed disclosure requirement to highlight risks of intellectual property infringement in the Summary and Risk Factors sections of the prospectus. We also note the requirement for the prospectus to include a positive statement by the directors (supported by the sponsor's due diligence) as to whether the applicant has infringed any third party intellectual property rights (with details) and, if applicable, assessing the potential impact on the applicant's operations (page V-19 of Appendix V). In relation to the first part of this proposed disclosure requirement, while a discussion of (i) the prevalence of litigation in a particular industry area, (ii) which industry operators hold significant concentrations of patents, and (iii) historic litigation trends in the industry area and the relevant geographies, etc may be helpful to an investor in assessing the risk profile of a listing applicant, there is a concern that listing applicants would be cautious about providing specific disclosure in relation to their own infringement position.

	In this regard, we would suggest that the Exchange provide further guidance on the disclosure requirements to avoid overly generalised risk factors being put forward that do not provide investors with specific information about the actual intellectual property risks that a particular listing applicant following the listing. In relation to the second part of this proposed disclosure requirement, the Exchange should note that intellectual property infringement analysis requires a highly technical and complex assessment and infringement will not likely be established one way or the other until a court gives its ruling on the matter. Accordingly, it may not be possible for directors to provide a positive confirmation as to whether there has been infringement and in some cases, the giving of such confirmation in the prospectus could potentially prejudice the listing applicant's legal position in the event of a dispute.
Questions 41:	**Do you agree that the controlling shareholders of a Specialist Technology Company should be subject to a lock-up period of (a) 12 months (for a Commercial Company) and (b) 24 months (for a Pre-Commercial Company)?** **Please give reasons for your views.**
A:	We agree with the respective lock-up periods for controlling shareholders in a Commercial Company and a Pre-Commercial Company. These more stringent lock-up periods than that currently imposed on controlling shareholders can send a signal to the market that the controlling shareholders are more committed to the long-term prospect of the listing applicant which is likely to be at the early stage of its development cycle. We note that these lock-up periods are significantly more relaxed than those issuers listed on the STAR Market whereby pre-IPO securities held by controlling shareholders and de facto controllers are subject to lock-up period of 36 months from the date of listing, and for issuers without any profit at listing, such lock-up period can be extended to three full financial years from listing (or until the issuer makes a profit). The difference in the lock-up periods on controlling shareholders may have the effect of encouraging primary listings in Hong Kong or dual listings in mainland China and Hong Kong. If the Exchange's intention is to also attract STAR board listed companies to list under the proposed new listing regime for Specialist Technology Companies, the Exchange should issue some guidance on dual-listings under the proposed Chapter 18C of the Listing Rules in its guidance letter. In connection with this, we would also like to suggest that the Exchange should consider the feasibility of including Specialist Technology Companies into the SH-HK/SZ-HK Stock Connect regime. We are of the view that the availability of southbound trading into Specialist Technology Companies will greatly enhance the attractiveness of the new listing regime to potential listing applicants.