Issue 11 I November 2024

Listing Regulation and Enforcement Newsletter

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Welcome to this newsletter! Following recent organisational changes within the Listing Division, this publication is now called the Listing Regulation and Enforcement Newsletter. It will continue to be published semi-annually, as we keep you updated on our regulatory developments and support you on your compliance journey.

Introducing the Listing Regulation and Enforcement department

Effective 1 October this year, the Listed Issuer Regulation and Listing Enforcement departments have merged to form a new department called Listing Regulation and Enforcement (**LRE**). In the past, both departments handled post-listing compliance matters of issuers, with different focus and scope. The integration seeks to maximise synergies to enhance efficiency, capability and responsiveness. The merger will facilitate a more holistic approach to the end-to-end process, including ongoing monitoring, non-compliance identification, investigation, disciplinary and enforcement and issuer education, to achieve more timely and desirable regulatory outcomes, as well as stronger market education and deterrent effect.

Going forward, LRE will continue to review and refine its approach to ensure it continues to serve its purpose and protect the integrity and reputation of our market and Hong Kong as an international financial centre.

Convertible bond offerings with concurrent share buyback

This year, there has been a surge in the issuance of convertible bonds (**CBs**) by listed issuers. Of note, some secondary-listed issuers with large market capitalisation and good liquidity have undertaken concurrent share buyback along with their CB offerings. To further enhance the competitiveness of our market, we have engaged with market participants and explored whether primary-listed issuers may leverage on this structure.

As background, professional investors such as hedge funds and arbitrage investors are the main investor groups in CB offerings. In line with their investment strategies, they would hedge their exposure under the CBs by short-selling shares of the issuers. From time to time, issuers in overseas markets (for instance the United States) would purchase the shorted shares to facilitate the investors' hedging. This concurrent share buyback would not only enable investors' participation in the CB offerings, but, more importantly, ease the downward pressure on the share price due to creation of short position through the short-selling activities that coincide with the CB offerings.

Regarding primary-listed issuers, such a concurrent share buyback would fall within the scope of Rule 10.06(3). Under the Rule, an issuer may not issue any new shares within 30 days of a share buyback, unless with the Exchange's prior consent. This Rule aims to ensure that the issuance price of the shares has not been affected by the share buyback.

We welcome primary-listed issuers to consult us on any proposed concurrent share buyback at an early stage, so that we can assess the specific circumstances on a case-by-case basis and provide our prompt feedback.

Update on listing fee payment process and arrangement

Under the Fee Rules, listed issuers are required to pay subsequent issue fee and/or transaction related fees and levies[1] for issuance of securities depending on the structure of their equity fundraisings. To enhance consistency and provide more transparency on how listing fees and related fees and levies are derived, effective from December 2024:

- our debit notes to listed issuers will cover not only subsequent issue fee payable but also related fees and levies; and
- if the listing ultimately results in the payment of a reduced fee, we will offset the balance from the excess fee paid against a future fee payable by the listed issuer.

Going forward, we will continue to refine the listing fee payment process and arrangement.

The delisting Rules six years on

A little over six years ago, the Exchange updated its Rules to establish a delisting framework (**Delisting Framework**) to address the issue of prolonged suspension of trading in issuers' listed securities. In this time, we are glad that the Delisting Framework has met its objectives, improving transparency to investors and raising market quality. We are also encouraged by the support of the Court which has consistently endorsed the Exchange's approach to handling long suspended issuers under the Delisting Framework.

Background of the Delisting Framework

Prior to the Delisting Framework, the then-applicable Rules focused only on requiring suspended issuers to take steps to resume trading. Suspended issuers therefore could remain suspended for a prolonged period without the prospect or certainty of trading resumption or delisting. This situation affected the proper functioning of the market.

On 1 August 2018, the Delisting Framework took effect. It was designed to address the issues of prolonged trading suspensions and to maintain market quality and reputation, with the following specific objectives:

- To facilitate an orderly exit for issuers that no longer meet the continuing listing criteria.
- To provide certainty to the market on the delisting process and enable the Exchange to meet its statutory obligation to maintain a fair, orderly and informed market for the trading of securities.
- To incentivise suspended issuers to act promptly towards resumption.

Under the Delisting Framework, issuers who fail to remedy issues and resume trading within a prescribed period (18 months for Main Board issuers and 12 months for GEM issuers, **Remedial Period**) can be delisted. The Remedial Period will not normally be extended unless an issuer can satisfy the Exchange the existence of "exceptional circumstances" as described in Guidance Letter **GL95-18**.[2]

[1] Including SFC transaction levy, AFRC transaction levy, trading fee and brokerage.

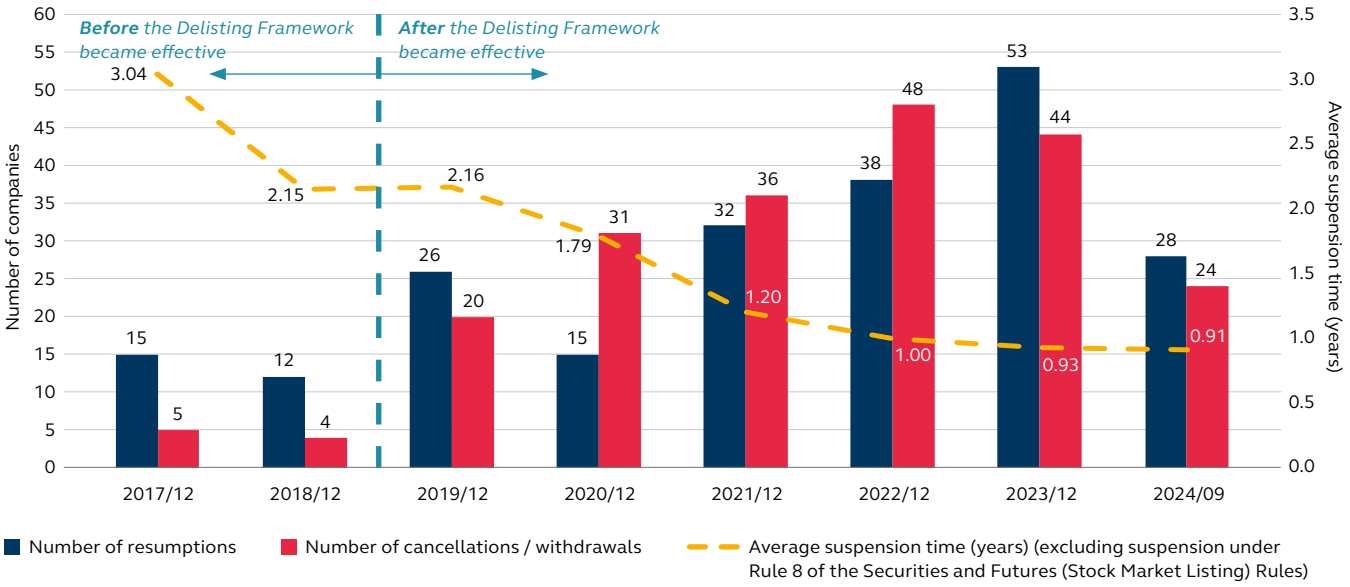
[2] "Exceptional circumstances" are defined in paragraph 22 of guidance letter GL95-18, requiring that (a) an issuer has substantially implemented the steps that, it has shown with sufficient certainty, will lead to resumption of trading; but (b) due to factors outside its control (expected to be procedural in nature only), it becomes unable to meet its planned timeframe and requires a short extension of time. Paragraph 23 of GL95-18 further confirms that even if there are factors outside the issuer's control, the Exchange does not have to consider such situation "exceptional", in particular if it is unclear whether (a) the issuer took adequate action and acted promptly throughout the Remedial Period, and (b) there is sufficient certainty that the issuer will be able to comply with all resumption conditions/guidance within the requested extension of the Remedial Period.

Results of the Delisting Framework

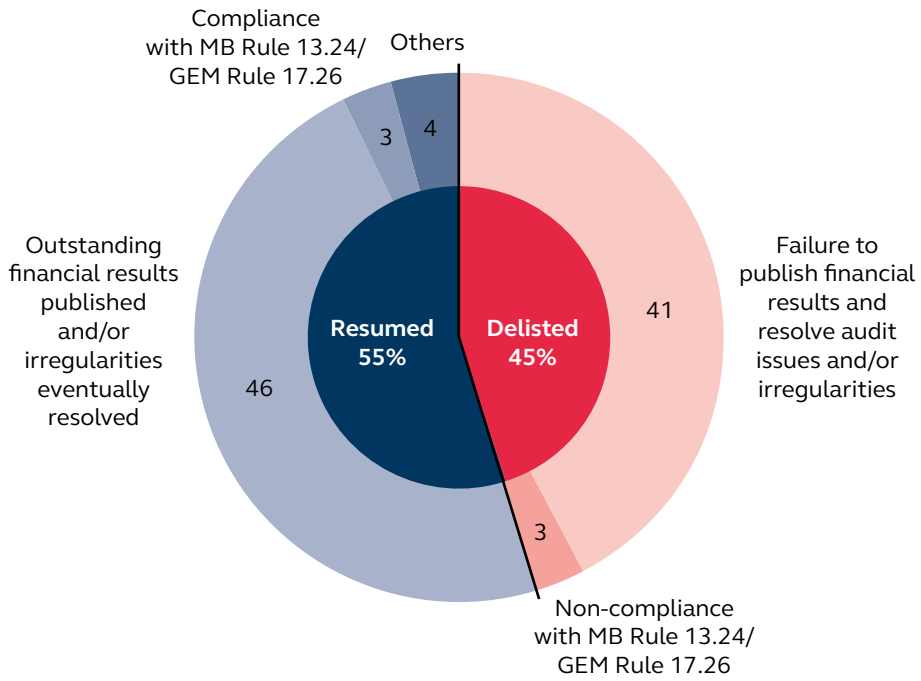
The Delisting Framework has achieved its objectives and raised market quality, notably:

- **More resumption than delisting:** In 2023 and the first nine months of 2024, more long suspended companies resumed trading than were delisted.
- **Substantial reduction in average time of issuers staying suspended:** from over three years in 2017 (the last full year before the Delisting Framework became effective) to less than one year in 2023.

Statistics of long suspended issuers before and after the Delisting Framework became effective



In 2023, the Exchange handled 97 long suspension cases, of which 53 issuers resumed trading and 44 were delisted. The chart below shows the reasons for their resumption/delisting.



Delisting decisions

Delisting decisions are made by the Listing Committee (**LC**) and, insofar an issuer applies for a review of the LC's decision, reviewed by the Listing Review Committee (**LRC**).

Statistics of delisting decisions made by the LC and reviewed by the LRC

	Year ended 31 December					Nine months ended 30 September
Year	**2019**	**2020**	**2021**	**2022**	**2023**	**2024**
Delisting decisions made by the LC	25	36	27	56	46	15
Delisting decisions reviewed by the LRC[3]	17	22	12	16	16	7
- Upheld	*15*	*21*	*12*	*12*	*14*	*7*
- Overturned	*2*	*1*	*0*	*4*	*2*	*0*

[3] This refers to the delisting decisions made by the LC during the year which were subsequently reviewed by the LRC. Some of the review hearings may not take place within the same year.

Court recognition

Once the LRC has made a final delisting decision, an issuer can only challenge such decision through the Court[4] by way of a judicial review. Since the Delisting Framework took effect, several issuers have taken out applications for judicial review.

The scope of these applications is limited to a few narrow grounds, including that (i) refusing to extend the Remedial Period and/or (ii) delisting of the issuer's securities was unreasonable in a public law sense or an improper exercise of the Exchange's discretion.

None of these applications has prevailed.[5] The Court has regularly endorsed the Exchange's Delisting Framework and approach to handling time extension requests. A selection of the Court's reasons is summarised below:

Extensions of the Remedial Period is only possible on very narrow grounds

The Court confirmed the Exchange's approach in interpreting the Remedial Period strictly and granting extensions only in "exceptional circumstances" which the Exchange considers warrant a time extension. In particular:

(i) The Court recognised that the Delisting Framework is intended to enable the Exchange to meet its statutory obligation to maintain a fair, orderly and informed market for the trading of securities.[6]

(ii) The Court confirmed that a suspended issuer has the primary responsibility to devise its own resumption plan to remedy the relevant issues before the Remedial Period ends to avoid delisting. For demonstrating compliance with the Exchange's resumption conditions/guidance, the issuer assumes the responsibility to ensure that the materials which it considers material are placed before the Exchange and in a timely manner. The Exchange is not obliged to make further general enquiries, or to ask for potential documents not already provided by the issuer.[7]

(iii) The Court confirmed that what amounts to "exceptional circumstances" warranting a time extension is **a matter for the Exchange and not the Court to decide** – in reviewing such a decision, the Court's role is limited to assessing whether the Exchange's decision was irrational which the Court confirmed is a high hurdle to overcome.[8]

(iv) The Court **endorsed the forward-looking approach** of the Exchange in analysing whether a time extension is warranted, in that the Exchange is not obliged to consider circumstances "exceptional" only because the issuer's ability to substantially implement remedial steps was inhibited by factors outside its control – the Exchange is entitled to reject a time extension request if the issuer fails to demonstrate with sufficient certainty that it would be able to meet all of the Exchange's resumption conditions/guidance within the requested time extension.[9]

(v) The Court confirmed the Exchange's view that the appointment of liquidators does not in itself constitute "exceptional circumstances" warranting a time extension. In line with (iv) above, even if some exceptional circumstances are found to exist in such cases, the Exchange does not need to take a "wait and see" approach but has the discretion to refuse granting a time extension immediately on the basis that the issuer had failed to demonstrate with a sufficient degree of certainty that it would be able to resume trading within the requested extension.[10]

Exchange has the regulatory power to cancel listings

The Court confirmed that it is within the Exchange's regulatory powers to make a delisting decision, in particular that:

(i) It is open for the Exchange to take the view that the delisting of long suspended issuers under the Delisting Framework is overall beneficial to the public and the investing public as a whole, which may **balance and outweigh the harm resulting to the minority shareholders of any specific delisted issuer**.[11]

(ii) An issuer's listing status does not represent "property" under Article 105 of the Basic Law and a delisting decision therefore does not trigger the protections under the Basic Law.[12]

[4] An application for leave to apply for judicial review of a decision by the LRC must be launched in the High Court of the Hong Kong Special Administrative Region, Court of First Instance.

[5] Since the Delisting Framework took effect, 20 applications for judicial review against delisting decisions of the Exchange have been considered by the Court. In all these cases, the Court dismissed the applications with orders requiring the applicants to pay the Exchange's legal costs, or the applicants withdrew or discontinued such applications prior to the hearing.

[6] Cai Zhenrong vs The Stock Exchange of Hong Kong, [2021] HKCFI 1899; CIL Holdings Ltd vs The Stock Exchange of Hong Kong, [2023] HKCFI 1618.

[7] Sino Energy International Group Holdings Ltd vs The Stock Exchange of Hong Kong, [2022] FIKCFI 3409.

[8] Sino Energy, [2022] FIKCFI 3409; China Wood Optimization (Holding) Limited vs The Stock Exchange of Hong Kong, [2023] HKCFI 1000.

[9] China Wood Optimization, [2023] HKCFI 1000; see also paragraph 23 of GL95-18.

[10] Titan Petrochemicals Group Ltd vs The Stock Exchange of Hong Kong, [2023] HKCFI 2935.

[11] CIL Holdings, [2023] HKCFI 1618.

[12] Longrun Tea Group Company Limited vs The Stock Exchange of Hong Kong, [2021] HKCFI 1883.

Outlook

Based on the results of the Delisting Framework and the endorsement from the Court, the Exchange will continue to pursue the objectives of the Delisting Framework: keeping trading suspensions to a minimum to maintain a fair, orderly and informed market for the trading of securities, and incentivising suspended issuers to act promptly towards resumption.

Important reminders for suspended issuers and their boards

It is the suspended issuer's primary responsibility to promptly formulate and execute remedial action plan for resumption of trading, bearing in mind the time-criticalness under the Delisting Framework. Below, we summarise areas to which they should pay attention with a view to helping them navigate regulatory issues along their resumption journey. When in doubt, issuers should seek guidance from our designated officers or solicit professional advice.

- **Directors' continuing obligations to procure suspended issuers to comply with the Rules and act promptly and proactively throughout the Remedial Period to remedy any issues for a resumption of trading**

  Despite the clear objectives of the Delisting Framework, the Exchange still observes cases where suspended issuers do not appear to take prompt and adequate action to remedy issues and resume trading. This can result in undue delay in the resumption of trading or, for those failing to resume trading within the Remedial Period, delisting.

  Directors are reminded that while trading in an issuer's shares is suspended, they remain required to comply, and procure the issuer to comply, with the Rules. They should therefore apply due skill, care and diligence and act promptly to procure the issuers to re-comply with the Rules and resume trading as soon as possible and, in any event, within the Remedial Period to maintain their listing status. Failure to do so can lead to disciplinary action against the directors, which may result in the imposition of public sanction under the Rules.

  When in doubt, directors should seek professional advice promptly.

- **Keep market appropriately informed of business operations and resumption progress during suspension**

  Following their suspension, some issuers announce very limited information about their business operations and resumption progress. This causes potential uncertainty and a lack of transparency in the market and among the issuers' shareholders. Further, a lack of meaningful announcements could be indicative of the issuers' failure to act promptly and adequately towards a resumption of trading and could be a factor against the Exchange granting an extension of the Remedial Period, if requested. Directors are reminded to procure a suspended issuer to announce quarterly updates on its business operations and detailing the progress of implementing its resumption plan and satisfying the resumption conditions/guidance (including the reasons for, and impact of, any delay), as required under MB Rule 13.24A / GEM Rule 17.26A and paragraph 11(d) of guidance letter (GL95-18).

- **Reviews of the LC's delisting decisions by the LRC will be processed without delay**

  Issuers subject to a delisting decision by the LC can apply for a review of this decision by the LRC. They should note, however, that such review application will be conducted expediently and that the review process is not intended to provide them with additional time to comply with the resumption conditions/guidance. Following a review application to the LRC, issuers will be expected to provide a written submission together with the grounds for review within five business days of the submission of their review application. The Secretary of the LRC will schedule a hearing date as soon as possible after receiving a review application.

- **Keep abreast of relevant guidance from the Exchange**

  To ensure prompt and adequate steps for trading resumption are taken, issuers and their boards should closely follow guidance issued by the Exchange from time to time. Such guidance (such as the below guidance letters) can assist suspended issuers and their boards in assessing what steps they must undertake and what the Exchange's expectations are.

Guidance Letter	Topic / Relevance
GL95-18	Long suspension and delisting
GL96-18	Suitability for continued listing, particularly guidance on shell companies and prolonged suspension
GL104-19	Guidance on application of the reverse takeover Rules
GL106-19	Guidance on sufficiency of operations
GL120-24	Guidance on investigations conducted by long suspended issuers

Reminders on planning for upcoming audit

In just a few months, issuers with a December financial year-end will be due to publish their 2024 annual accounts. By now, we believe many of these issuers are already finalising their audit plans, including agreeing on major processes and timelines with their auditors.

Evaluating audit quality

A quality audit plays a vital role in a listed issuer's accurate and timely financial reporting in discharge of its Rule obligations. Under the Corporate Governance Code,[13] audit committees shoulder the responsibility for recommending appointment, reappointment and removal of external auditors to the board. Such recommendations are based on factors including the auditors' ethics, knowledge, experience and capacity – all of which affect the quality of the audit.

We noted recent instances where the auditors were sanctioned by regulatory authorities for failing to comply with certain reporting obligations or to identify material misstatements in issuers' financial statements from their audit procedures. We take this opportunity to remind audit committees to take such regulatory instances into consideration when evaluating the auditors' audit quality in a due and timely fashion. Any late change in auditors, if necessary, might result in the issuers missing the reporting deadline. In addition, issuers should consider the material misstatements or irregularities identified by the regulatory authorities and their relevance to the issuers' circumstances. If necessary, they should make rectifications and enhancements in the controls over their financial reporting process promptly.

Ultimate responsibility for the integrity of accounts rests on issuers and their board of directors

Despite the important check-and-balance role played by external auditors, we emphasise that issuers themselves bear the ultimate responsibility for the integrity of their accounts and reporting systems. They are primarily responsible for presenting financial statements with a balanced, clear and comprehensive assessment of their performances. To achieve this, directors must do their best to procure the issuers to build and maintain effective financial reporting systems, while audit committees must diligently discharge their supervisory function over the integrity of the financial statements and financial reporting systems overall.

Issuers are encouraged to visit our previous newsletters[14] and publications released by the AFRC for more guidance on (i) selecting auditors[15] and (ii) planning and conducting an effective audit.[16]

We are reviewing issuers' annual reports published in 2023. Financial reporting and related controls remain one of our core review themes. Issuers are encouraged to read our report, expected to be published next month, for our findings and recommendations on preparing financial statements.

Designation of authorised representatives

Authorised representatives serve as the principal channel of communication between issuers and the Exchange[17] and, from time to time, we make time-critical enquiries with issuers that require prompt response. For example, when unusual movements in the trading price or volume of the issuer's shares are observed, we might contact the authorised representatives to seek confirmation on whether there is inside information that needs to be disclosed. In that case, a prompt assessment and response by the issuer is crucial in effecting a swift trading halt where necessary to preserve a fair and orderly market. In our November 2023 **Newsletter**, we reminded issuers to ensure their designated authorised representatives are contactable at all times.

In addition to reachability, we have recently observed issues in isolated cases where the authorised representatives took a lengthy period to revert with the issuers' assessment and position. In our view, the long response time reflected a lack of familiarity of the authorised representatives with the issuers' daily operations and business affairs and/or direct access to the board.

In this connection, we encourage issuers to review their authorised representative designation from time to time to ensure the designates have a good understanding of the issuers' latest developments, ready access to the board and senior officers of the issuers, and the necessary authority to make representations to the Exchange and decisions. Issuers should ensure effective and efficient communication channels and protocols are in place to facilitate prompt engagement and discussion between board members and relevant officers of the issuers on the subject matter of enquiries.

[13] Code Provision D.3.3(a) of Appendix C1 to MB Rules / Appendix C1 to GEM Rules.

[14] December 2020 **Newsletter**, December 2021 **Newsletter**, and November 2023 **Newsletter**.

[15] **Guidelines for Effective Audit Committees – Selection, Appointment and Reappointment of Auditors** and **Safeguarding Auditor Independence: Concerns Surrounding Procurement and Purchases from Audit Clients**.

[16] **Audit Focus for 2024 year-end audits** and **Audit implications of current economic conditions for Hong Kong-listed companies**.

[17] MB Rule 3.06(1) / GEM Rule 5.25(3).

Gender diversity on boards – The clock is ticking!

Diversity has been and will continue to be a key focus of the Exchange. The deadline of 31 December 2024 to appoint at least one director of a different gender on the board is end of next month. To date, a small number of listed issuers still have a single-gender board – we urge these issuers to act promptly to comply with the Rule before the deadline.

Publications

We have recently published or revised the following guidance materials:

- Updates of guides, FAQs, guidance letters, listing decisions, checklists, forms and templates (7 June 2024) and e-Forms (8 June 2024) to reflect Rule amendments relating to the treasury share regime.
- New e-learning modules on (i) **Exchange's New Climate Requirements** (17 June 2024) to assist issuer in understanding, interpreting and implementing the new climate requirements; and (ii) **Preparing for ISSB Sustainability Disclosures** (24 September 2024) to provide practical guidance on the preparation of ISSB sustainability disclosures.
- A **joint announcement** of the SFC and the Exchange (23 August 2024) in relation to temporary modifications to requirements for Specialist Technology Companies and De-SPAC Transactions and updates of **Guide for New Listing Applicants**, **revised GL113-22** and **revised FAQ14.3 – No.1-13** (30 August 2024) to reflect the temporary modifications.
- Updates of guides, **revised FAQ11.2 - No.29** and **amendments to MB Rules** and **GEM Rules** relating to severe weather trading (20 September 2024).
- **Revised GL104-19** (20 September 2024) which incorporated a new case in the appendix (case 9) to illustrate how the Exchange applies the reverse takeover Rules in relation to an acquisition that formed part of the issuer's expansion strategies related to its existing business.
- Revised monthly return e-Forms (16 November 2024) for equity issuers, Hong Kong depositary receipts and collective investment schemes (Main Board issuers – **FF301/FF302** and GEM issuers – **FF301**).
- **2024 Analysis of ESG Practice Disclosure** (25 November 2024) to report the Exchange's assessment on the compliance of listed issuers' ESG reports with the ESG reporting framework.
- **GL120-24** (26 November 2024) to provide guidance on investigations conducted by long suspended issuers.
- **Revised GL95-18** (26 November 2024) to remove the guidance relating to COVID-19.

We have also recently published:

- A consultation paper on **Review of Corporate Governance Code and Related Listing Rules** (14 June 2024) to address current corporate governance concerns and areas where further improvement can be made.
- A consultation paper on **Proposals to Further Expand the Paperless Listing Regime and Other Rule Amendments** (16 August 2024) to expand the use of electronic channels to further enhance operational efficiencies and sustainability.

We welcome your feedback.
Please send your thoughts and comments to
listingnewsletter@hkex.com.hk