RESPONSE TO HKEX CONCEPT PAPER ON WEIGHTED VOTING RIGHTS

by

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Introduction

We have set out below our general comments on the issue of weighted voting rights (***WVRs***). We have categorised these into four areas: restrictions and limitations, investor rights, investor choice and investor protection. We are of the view that The Stock Exchange of Hong Kong Limited (the ***Exchange***) should allow companies to list with WVRs, subject to appropriate safeguards being in place to protect investors.

Restrictions and Limitations on WVR structures

We would expect the Exchange to impose various restrictions and limitations on the use of WVR structures to ensure that holders of special voting shares do not abuse their position. Where possible, these should be clearly outlined in the Listing Rules so that potential issuers are able to plan accordingly. Nevertheless, we also believe that the Exchange should have a high degree of flexibility to waive restrictions and limitations and to impose additional restrictions and limitations where it is appropriate to do so on a case by case basis so that they can be tailored in a way that ensures investor protection while not placing unduly onerous restrictions on issuers. We would make the following observations in relation to specific restrictions and limitations:

- We believe that WVRs should only be permitted for persons who are existing shareholders of a company at the time it carries out its IPO, that special voting shares should convert into ordinary shares on transfer, death, incapacity or bankruptcy of the holder, and that the percentage of total votes held by the special voting block should not be able to increase post IPO by further issues of special voting shares (unless there is a pro rata issue of ordinary shares at the same time so that the percentage of total votes is unchanged).

- We believe that WVRs should only be permitted for new applicants as we do not think that investors who had purchased shares in a one share one vote structure company should be exposed to the risk that the company adopts a WVR structure without their consent (e.g. because it can be adopted with a majority vote), resulting in them holding shares in a company with a WVR structure. This risk would not apply to new applicants because all investors would be investing in full knowledge that they are acquiring shares in a WVR company.

- We do not believe that the Exchange should limit WVR structures to dual class shares. The Exchange should take an open, flexible mind to WVR structures, evaluating them on the basis of whether the company is subject to sufficient investor protection requirements to outweigh the risks of the structure. For example, the partnership structure adopted by Alibaba is a good example of balancing board control with investor rights, since unlike a conventional dual class share structure, ordinary shareholders are able to remove directors appointed by the partnership at subsequent general meetings.

No Major Change to Investor Rights

Most of Hong Kong's listed companies are controlled companies. When we invest in such a company, we are making a largely economic investment, investing on the basis of the company's business and its management team, knowing that we have very limited influence,

acting alone or with other investors, to make changes to either of those things. This is essentially the same as investing in a company with a WVR structure, and we do not consider that we would be any worse off as an investor in such a company from an investor rights point of view. Moreover, given Hong Kong and China based investors are highly experienced in dealing with controlled companies and the risks that they present, we think that they would be well placed to evaluate companies with WVR structures and the associated risks.

Investor Choice

We consider that the Exchange should permit companies to list with WVRs so that Hong Kong and China based investors are able to invest in such companies if they wish to do so. A ban on WVRs means that many Hong Kong and China based investors are unable to invest in many of China's leading new companies or are forced to do so in the secondary market through an overseas stock exchange, generally the New York Stock Exchange or NASDAQ. This harms Hong Kong and China based investors in a number of ways:

- It can be difficult for Hong Kong and China based institutional investors to obtain an allocation in the initial public offerings of such companies and generally impossible for retail investors to do so.

- Where it is not possible to obtain an allocation, investors are forced to purchase in the secondary market, which will often only be possible at a considerable premium to the IPO offer price, as has been demonstrated by a number of recent large IPOs, such as Alibaba and JD.com. This reduces Hong Kong and China based investors' potential returns.

- Even where it is possible to obtain an allocation on an offering, it will typically result in the investor paying higher charges than it would if the offering were made in Hong Kong due to the need to invest on an overseas market and trade in US$ rather than HK$.

- Many retail investors will not be able to invest at all (i.e. even in the secondary market) since they will not have the ability to purchase non-Hong Kong stocks. For these investors, they are completely denied the ability to share in the potential growth of these companies.

Investor Protection

Even if Hong Kong and China based investors are able to purchase shares in a company with WVRs on an overseas market, they will generally be subject to much weaker protection against abuse of those WVRs than they would if the shares were listed in Hong Kong. In particular:

- The Exchange and SFC both have considerably experience of dealing with PRC issuers, variable interest entities and controlled companies, and are arguably better placed to regulate Chinese companies with WVRs than regulators in the United States or elsewhere.
- Hong Kong has a well-established regulatory framework for regulating companies with shareholders who control a majority of the votes of the company (i.e. controlled

companies), since most of the companies listed in Hong Kong are controlled companies. In particular, Hong Kong has an extensive and detailed set of rules for connected transactions, which guards against the extraction of private benefits by connected persons, including substantial shareholders and directors, at the expense of other shareholders. No equivalent rules exist in the United States and no other overseas markets have rules that are as extensive as those in Hong Kong.

- If a Hong Kong or China based investor has a grievance with an issuer or its directors or advisers, it can easily approach the Exchange and SFC and ask them to pursue its claim, or make a claim itself in the Hong Kong courts. The SFC has used its powers in a number of recent high profile cases involving listed companies and obtained significant sums in compensation for investors. It is typically considerably more difficult for a Hong Kong or China based investor to seek redress against an issuer listed overseas and the home regulator may be less inclined to pursue the claim.

Concluding Remarks

The Exchange has demonstrated many times over the past few decades that it has the capacity to amend its rules to provide investors with the ability to participate in new developments in the equity capital markets. For example:

- In 1993, Hong Kong listed the first H share company, and the Listing Rules have a dedicated chapter for the listing of PRC companies.

- In 2007, Hong Kong implemented a framework to allow the listing of overseas companies, which was further refined in 2013, and it now allows companies incorporated in 24 overseas jurisdictions to list on the Exchange.

- Hong Kong has permitted the listing of companies using 'variable interest entities' (***VIEs***) for many years and imposes strict limitations on the scope of VIEs and requirements for the associated shareholder protections.

We believe that allowing the listing of companies with WVRs would be a logical step in Hong Kong's continuing development and that the Exchange is more than able to do this in a way that ensures that investors are adequately protected, as it has demonstrated in the past. Permitting WVR structures would enable Hong Kong and China based investors to participate in many of the successful new businesses coming out of China, which they are currently unable do or only at to do at greater cost and without the benefit of the Hong Kong regulatory regime. By not allowing WVR structures in Hong Kong, Hong Kong and China based investors are being disadvantaged on the global stage.