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Consultation Paper
A Listing Regime for Companies from Emerging and Innovative Sectors

Comments from Shearman & Sterling

We set out below our comments in relation to the proposals set out in the Consultation Paper on "A Listing Regime for Companies from Emerging and Innovative Sectors" issued by The Stock Exchange of Hong Kong Limited (the "**Exchange**"). We are broadly supportive of each of the three key proposals in the Consultation Paper. We believe that the goals of keeping up with the market developments and maintaining high regulatory standards are not necessarily mutually exclusive.

Our comments are geared toward the new Chapter 18A. As the Exchange is aware, we were part of the core team that successfully brought Wuxi Biologics (2269.HK) to the Hong Kong capital markets and we continue to actively drive a number of biologics and CRO related applications that will further shore up our leading position in this field.

Unless the context otherwise requires, terms used below have the same meanings as defined in the Consultation Paper or, where applicable, in the draft amendments to the Listing Rules set out in Appendix I to the Consultation Paper.

(A) Biotech Companies

1. **Biotech Product definition:** As drafted, the term encompasses all forms of "biotech products, processes or technologies". Presumably the relaxation from strict Financial Eligibility Tests is designed to address the acute funding needs associated with the development of biotech products (typically a protracted process from discovery to commercial launch) and oftentimes the massive capital required of the full cycle. The same challenges may not necessarily apply to companies focusing on processes or technologies, whose capital demands to support their R&D efforts could be far less intensive. They may not be subject to FDA or equivalent validations or successive clinical trials that are required of a product candidate. The minimum expected market cap at HK$1.5 billion should already disentitle a significant number of early stage players that would otherwise benefit from the relaxation. It is still felt that only those R&D heavy and long product cycle biotech companies should legitimately stand to benefit from adjusted financial tests. Please note that this comment should not be taken to keep out process- and technology-driven biotech companies from the new chapter.

2. **Milestones:** The entry point is conveniently referenced against the FDA (or near equivalent) approval process. While it gives investors a frame of reference in determining where the development progress falls, the initial approval process has little bearing on the prospects of product development and commercialization. Passing muster with Phase I clinical trials and getting set for Phase II could be taken by the investing public as an indicative measure of likelihood of success in the Core Product development or commercialization. We recommend that a more advanced stage of FDA or its equivalent be stipulated to lessen the risk of the Core Product launch not materializing eventually. A detailed due diligence trail including a description and analysis of the design of the clinical trials, trial size, statistical package, pre IND meeting memoranda, investigational plans, filings with and reports to the FDA should be separately complied by sponsor as part of the broader PN21 requirements, and be made available to the Exchange upon request. We agree the suggested disclaimer will help.

3. **Track Record:** Especially if we consider only a more advanced stage to be eligible for the new Chapter 18A, then the shorter track record of two financial years may not be warranted. Unlikely a Core Product would take less than two financial years to meet the requisite stage of development.

4. **Durable patents and IPRs:** If "durable" means "sustainable", the Exchange may consider a broader and deeper disclosure approach, giving details of inventions, patentable or otherwise proprietary, licensing in and out terms, prosecution history ("file wrappers"). The term "durable" is fraught with ambiguity, and it would be somewhat challenging to prove biotech IPRs to be durable.

5. **Efficacy and safety:** This should be covered both in the industry report, as much as the product specific disclosure. The diligence efforts could be varied and somewhat horrendous if taken to the highest level. The Exchange's guidance on diligence level expected will be much appreciated. We will be happy to share our views drawn from our wide experience advising bulge bracket sponsors in this field.

6. **Restrictions on Cornerstones:** This seems out of place when we are looking at companies with a market cap of HK$1.5 billion. Given the requirement of a minimum 25% public float, the market capitalization of shares held by the public would be at least HK$375 million, as compared to HK$125 million required under rule 8.09(1). With the increased market capitalization, the issue of an "open market" should be of lesser concern for Biotech Companies listed under Chapter 18A. If restrictions are to be introduced, we should do a holistic review of all segments (as the regulators did in previous years) rather than targeting this new chapter. Please also confirm/clarify whether it is possible for a Biotech Company seeking a listing under Chapter 18A to apply for a lower percentage of minimum public float under rule 8.08(1)(d) if its expected market capitalization is over HK$10 billion.

(B) Weighted voting rights

Draft rules 8A.22 and 8A.41: It is provided in draft rule 8A.41 that an issuer with a WVR structure must disclose any dilution impact of a potential conversion of WVR shares into ordinary shares in its listing documents and in its interim and annual reports. Given any conversion of shares with weighted voting rights into ordinary shares must occur on a one to one ratio according to draft rule 8A.22, is there any other dilution impact which is intended to be covered under draft rule 8A.41?

(C) Secondary listing

Equivalent standards of shareholder protection: It is not easy to understand draft rules 19C.06, 19C.07 and 19C.08 without knowing how the requirements under Appendix 3, Appendix 13, the 2013 JPS and the secondary listing rules in Chapter 19 work under the existing regime. Given secondary listing will not be governed under one single Chapter in the Listing Rules, it would be helpful if the Exchange could set out in the guidance letter a summary setting out the rules (in particular the requirements for "equivalent standards of shareholder protection") applicable to:

(a) secondary listing under the existing regime:

- Issuer incorporated in one of the recognized jurisdictions (i.e. Hong Kong, the PRC, Bermuda and the Cayman Islands); and

- Issuer incorporated outside a recognized jurisdiction;

(b) secondary listing under the new concessionary route (highlighting differences, if any, on the rules applicable to applicants incorporated within/outside the recognized jurisdictions):

- Non-Grandfathered Greater China Issuer;
- Grandfathered Greater China Issuer; and
- Non-Greater China Issuer.

We also set out below some questions/comments on the draft rules:

1) Is it necessary for a Non-Greater China Issuer or a Grandfathered Greater China Issuer incorporated in a recognized jurisdiction to demonstrate compliance with the shareholder protection standards in draft rule 19C.07?

2) If note 2 to draft rule 19C.06 (applicable to a Non-Grandfathered Greater China Issuer which is not incorporated in a recognized jurisdiction) and draft rule 19C.08 (applicable to a Non-Greater China Issuer or a Grandfathered Greater China Issuer) provide, in substance, for the same standards of shareholder protection, would it help to simplify the rules if:
   - Draft rule 19C.06 is revised to set out the requirement applicable to Non-Grandfathered Greater China Issuer incorporated in a recognized jurisdiction; and
   - Draft rules 19C.07 and 19C.08 be amended to set out the shareholder protection standards applicable to all other Qualifying Issuers?

Shearman & Sterling
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