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By email: [response@hkex.com.hk](mailto:response@hkex.com.hk)

London, 23 March 2018

**Re: Emerging and Innovative Companies CP**

**Consultation Paper:**

**A listing Regime for Companies from Emerging and Innovative Sectors**

Dear Sirs,

GES is a leading service provider of engagement services to institutional investors globally. Representing more than EUR 1 trillion of investments worldwide, GES acts as an owner advocate by assessing and engaging with clients' portfolio companies and reporting and providing related recommendations to investors.

GES is dedicated to good stewardship. We take seriously our clients' responsibility to exercise their ownership rights globally, particularly through voting their shares at all the general meetings at companies in their portfolios and engaging with companies.

GES welcomes the opportunity to respond to the consultation on proposed amendments to the Rules to allow the listing on the Main Board of (a) Biotech companies that do not meet any of the Financial Eligibility Tests including companies that do not have any prior record of revenue or profit (b) high growth and innovative companies that have WVR structures, and (c) Qualifying Issuers seeking a secondary listing on the Exchange.

Below are our comments.

**Biotech Companies**

Overall, we find the proposals related to biotech companies rather sound.

Rather than proposing that the company must have been engaged with the R&D of its core product(s) for a minimum of 12 months prior to listing, investors would be further reassured if this period was extended to 18 months.

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## Issuers with WVR structures

Our main concerns relate to WVR structures.

We note a resurgence in the use of different ownership and control mechanisms in various markets (including France, Italy, Brazil, United States etc) due to a number of factors ranging from the need for economic growth to the increase of technology company listings.

As the Exchange points out, the most common form of WVR structure used by companies listed in the United States is a dual class structure. However, the regulatory environment in the United States is different than that of Hong Kong. In particular, the United States Securities and Exchange Commission (SEC), does have authority to enforce securities laws and regulate the securities industry. It is our understanding that in Hong Kong, the SFC does not possess similar authority. In addition, HKEX's dual role as a market player and a regulator creates a conflict of interest (*see also our comment re. enforcement by Exchange*)

Shareholders in the United States can initiate class actions against potential management and board misconducts. It is also our understanding that the SEC is entitled to launch directors or shareholders who are deemed to have manipulated WVR structures. These options are strong protections for minority shareholders. In Hong Kong, however, filing class actions lawsuits is not an option available to shareholders.

GES' positions are guided by the ICGN Global Governance Principles and the ICGN Global Stewardship Principle, policies to which GES adheres as a member.

GES advocates a preference for the "one share, one vote standard.

Whilst we welcome the Exchange proposals on limits on WVR powers, protecting non-WVR shareholders rights vote, enhanced disclosure and enhanced corporate governance, we remain concerned that the control mechanisms through weighted voting rights are disproportionate when compared to their economic interests and cash flow rights. Equally, controlled entities with different voting rights can also have an effect on how management's incentives are aligned with shareholder returns and even actually encourage short-term behaviour by reducing the incentive for dialogue between the company and its investors.

*"A company controlled through weighted voting rights"* inevitably creates a misalignment between the economic interest in the company and the power to influence the strategy. There is, in addition, no evidence that suggests that companies in high growth/innovative sectors with a WVR structure provide over the long-term a superior environment for planning and execution.

As mentioned above, the safeguards proposed by the Exchange merit consideration; however, there is no evidence that they will act as effective checks and balances and act as guardians of minority shareholder interests against entrenchment and expropriation risks.

In our view, only companies with equal voting rights provide the right alignment for all shareholders and reduce the investment risk without distorting the market.

### **Companies suitable to list a WVR structure:**

GES would welcome further guidance on what happens when a new and *"innovative" business model may cease to be so if it is adopted by numerous industry players over time*". Should investors expect that in such cases, the Exchange would then require from the company that it abolishes its WRR structure or even delist?

**External validation:**

GES would welcome a clear definition of what a “*meaningful*” third party” investment. In addition, requiring such investors to retain an aggregate 50% of their investment at the time of listing for a period of at least six months post-IPO is too short. We advocate that investors retain their investment for a minimum period of 2 years.

**WVR Beneficiaries:**

We welcome the restrictions to the WVRs attached to beneficiaries’ rights.

As an additional minority investor protection risk and corresponding safeguard, we would welcome the adoption of a sunset provision. Such a clause would be implemented after a pre-determined period of time, at latest 5 years after listing.

**Protecting Non-WVR Shareholders Rights to Vote:**

*“The Exchange will require that a listed issuer’s WVR structure must enable Non-WVR Shareholders to cast at least 10% of the votes that are eligible to be cast on resolutions at the listed issuer’s general meetings. (see Appendix I, Rule 8A.09). The Exchange will also require that Non-WVR Shareholders holding at least 10% of the voting rights on a one-share one-vote basis (or such lower threshold as required under the laws of incorporation of the issuer) must be able to convene a general meeting and to add resolutions to the meeting agenda”*

GES does not believe that such a provision effectively protects non-WVR shareholders. We believe that non-WVR shareholders should be entitled to – as a minimum – have sufficient voting power to block special resolutions (so at least 25% of the voting rights)

**Grandfathering:**

It is not clear to us why Swire Pacific Limited would be exempted. We believe that the obligations should apply to all companies with a WVR structure.

**Corporate WVR Beneficiaries:**

Corporates should not be allowed to hold WVRs and there is no justification for a corporate shareholder that controls and consolidates the listing applicant as a subsidiary prior to listing to seek WVRs.

**Enforcement by the Exchange:**

A number of the the WVR safeguards described rely on the enforcement by the HKEX. Whilst we welcome the Exchange’s attempts at developing protective measures, we are concerned by the conflicts of interests posed by Exchange’s role as a standard setter /regulator and a commercial entity.

**Secondary listings of qualifying issuers**

An Overseas Issuers should only qualify for a secondary listing on the Main Board of HKEX under concessionary route if the standards and rules of its primary listing jurisdiction offer protections to investors that are at least equivalent to those required under the HKEX Listing Rules.

We recommend that HKEX issues detailed guidance in relation to the requirements and standard that Overseas Issuers would need to meet in order to be allowed qualify for a secondary listing in Hong Kong.

We hope our comments are helpful. If you have any further queries about our responses, please do not hesitate to contact us.

Yours sincerely,



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