



**CONSULTATION ON  
A LISTING REGIME FOR COMPANIES FROM  
EMERGING AND INNOVATIVE SECTORS**

**The Law Society's Submissions**

**The following is the Law Society's response to The Stock Exchange of Hong Kong Limited's consultation issued on 23 February 2018 on "A Listing Regime For Companies from Emerging and Innovative Sectors" (the "Consultation Paper"):**

Capitalized terms used but not defined herein have the meanings assigned to them in the Consultation Paper.

**1. Biotech Companies**

- 1.1 The Law Society supports the proposal to allow the listing of Biotech Companies with a minimum expected market capitalisation of HK\$1.5 billion, subject to enhanced disclosures in the prospectus and ongoing disclosures in the interim and annual reports.
- 1.2 We agree with a flexible definition of "Sophisticated Investor" since investment practices and structures are constantly evolving and a measure of discretion to allow regulators to apply a purposive approach is necessary. This should, however, be balanced against providing a degree of certainty to the market. An investor may, for example, need to know whether it fits the profile of a Sophisticated Investor under the Rules well before the listing process kicks off. In order that practitioners can advise their clients and the Exchange is not inundated with inquiries on an essential listing criterion, it is suggested that further guidance on the qualitative criteria of a Sophisticated Investor be provided such as, for example: (a) the investor would normally be required to have a minimum of HK\$[\*] million under management and with not more than [\*]% of its assets invested in the listing applicant; or (b) the size of the investment should be of a minimum amount,

subject of course to these criteria being indicative only and not undermining the Exchange's discretion to be exercised on a case by case basis.

- 1.3 The Exchange has consulted experts on the proposed definition of a Biotech company, Biotech regulatory approval bodies and the stages of regulatory approval for certain types of biotechnology products, processes and technologies. It is recommended that the Rules should recognise the continued role and support of these experts, at least during an initial period of say, 12 to 24 months, in order to give suitable assurance to the market that the Exchange and SFC will be assisted by experts in an area that may be outside their sphere of specialisation.

## 2. Issuers with WVR Structures

- 2.1 The Law Society supports the proposal to expand the listing regime to allow WVR structures to enhance the attractiveness of the Hong Kong market for quality and high growth companies.
- 2.2 We are not sure whether it is the intention of the Exchange that the numerical limits are not to be stretched to their limits. If not, the Exchange may need to clarify or re-consider some of the numerical limits/requirements. If the minimum economic interests of WVR beneficiaries is 10% and voting power of WVR is capped at 10 times, the minimum economic interests of 10% for WVR holders is not achievable if non WVR holders have to be given at least 10% votes:

If WVR = A (number of shares)

Non-WVR = B (number of shares) = 10% of voting rights

Total number of shares = A+B

$B/(A+B) = 1/10$

Hence:  $10B = A+B$ ;  $A=9B$  ;

$A < 10B$ ; and A will have less than 10% of the economic interests.

Likewise, if the maximum economic interest of WVR is 50% and voting power is capped at 10 times, then 50 WVR shares = 500 votes; 50 ordinary shares = 50 votes, and non WVR holders will have under 10% of voting power (50/550). If the above interpretation is correct, it seems the various requirements cannot all be

achievable: in the above examples, WVR shares can only achieve just under 10 times the votes, as one group, against the other group of non WVR shares.

- 2.3 The Exchange requires that Non-WVR holders to cast at least 10% of the votes. The definition of “Non-WVR Shareholder” refers to a shareholder who is not a beneficiary of WVR. A WVR holder may own both classes of shares. The Rules should state more clearly that the 10% requirement excludes the non WVR shares held by WVR beneficiaries, bearing in mind that non WVR shares may be held through different corporate and other complex structures. Another issue is whether the ordinary shares held by core connected persons of a WVR beneficiary can be counted towards the 10% vote.

2.4 **Lapse of WVR**

- (a) The rationale is that a beneficiary of WVR has made and will continue to make significant contribution. The requirement that the holder must remain a director should not be a token one. We consider that the holder must continue to have executive responsibilities and to have active participation in the issuer’s business and it is appropriate for INEDs to review annually whether beneficiaries of WVR have discharged executive functions in the listed group. We would like the Exchange to clarify its position as to whether non-executive Chairmen and non-executive directors can be beneficiaries of WVR if they contribute significantly to strategic development etc. of an issuer but are not involved in executive functions;
- (b) The Exchange should clarify if derivative agreements would be considered instruments that alter economic interests; and
- (c) There are many different forms of trust and tax planning arrangements. On the one hand, Rule 8A.12 seems impracticable as any transfer to a trust vehicle where the beneficiary relinquishes its direct control can be regarded as a circumvention of the restriction against transfer of weighted voting rights. While the Exchange allows limited partnerships and trusts to be used to hold WVR shares, there are no parameters or guidance on such structures. For example, is it acceptable for the founder/WVR beneficiary to set up a family trust to hold the WVR shares for his immediate family members if he is not a beneficiary? Is discretionary trust permitted? In the case of a limited partnership of a fund, does the WVR beneficiary have to be a general partner or can he simply be a limited partner? We think it would be helpful to clarify in the next consultation concerning corporate WVRs what is regarded as a suitable form of trust or limited partnership.
- (d) Consideration should be given to requiring a higher level of participation by INEDs at board deliberation and corporate/strategic decision making process, for

example requiring a higher majority of INED in board composition and presence of minimum number of INEDs to form quorum of a board meeting.

## 2.5 Corporate WVR Beneficiaries

We welcome the Exchange's confirmation that a further consultation will be conducted on allowing corporate beneficiaries of WVRs within three months of the implementation of a new Chapter 8A. As acknowledged in the Consultation Paper, this is a concern for stakeholders and it is thus clearly an issue to be examined in ensuring the optimum WVR structure for Hong Kong listings.

## 3. Secondary Listings of Qualifying Issuers

- 3.1 We agree with the proposal to create a new concessionary route to secondary listing for companies from emerging and innovative sectors that are primarily listed on a Qualifying Exchange, while preserving the important investor protection provisions under the existing regime.

## 4. Proposed amendments to the Listing Rules

- 4.1 The basic requirements of the listing of an applicant with a WVR structure set out in paragraph 106 of the Consultation Paper such as high growth, external validation, etc. is not embodied in the new Chapter 8A of the Listing Rules. In paragraph 106 (e), there is a requirement that a Sophisticated Investor for an issuer with WVR structure has to retain an aggregate of 50% of their investment for at least six months after listing. There is also a similar requirement for external validation from at least one Sophisticated Investor for Biotech Companies (paragraphs 8(g) and 74(g) of the Consultation Paper). We understand that flexibility is intended. It is, however, appropriate for certain key principles to be made into a listing rule while matters such as interpretation and circumstances for granting waivers, etc. can be governed by guidance letters.
- 4.2 Chapter 8A provides that save as modified, the requirements of Chapter 8 continue to apply to an issuer with a WVR structure. It is not exactly clear whether the requirement of "management continuity" for the three preceding financial years and "ownership continuity" for the most recent financial year continue to apply. The rationale for WVR is to allow greater management entrenchment over ownership. It seems that management continuity shall continue to apply. Is ownership continuity still relevant? We consider that this should be spelled out more clearly.

- 4.3 Ownership or holding arrangements permitted under Rule 8A.12 should be made subject to some form of vetting process by the Stock Exchange even if they are formed after IPO in the interest of giving certainty to validity of any such arrangements.
- 4.4 Rule 8A.12 refers to a limited partnership, trust, private company or other vehicle being able to hold WVR shares “on behalf of a beneficial owner” and Rule 8A.11 requires a WVR beneficiary to be a director. Is it intended that any holding structure must ensure that no one will benefit apart from the director himself?

**The Law Society of Hong Kong**  
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