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Confidential

Your reference: Corporate WVR CP
Our reference: [redacted]
Direct Dial: [redacted]

E-mail: [redacted]

Hong Kong Exchanges and Clearing Limited
8th Floor, Two Exchange Square
8 Connaught Place
Central
Hong Kong

27 April 2020

<u>Re: Corporate WVR CP</u>

Dear Sirs,

Responses to the Corporate WVR Consultation Paper

We are writing on behalf of our client, which is a listed company in Hong Kong, in response to SEHK's Consultation Paper on Corporate WVR Beneficiaries of January 2020 (the "**Paper**").

Unless otherwise indicated, the terms used in this letter shall have the same meaning as the Paper.

At the outset, our client welcomes and supports the general direction advocated by the SEHK in the Paper. In particular, our client agrees that the minimum HK$200 billion market capitalisation requirement, the "Innovative Company" related requirement, the "listing status" requirement and the 30% market capitalisation requirement as set out in Questions 15, 17, 18 and 19 respectively can help minimise floodgate concerns. It is also important for the market to recognise there should not be any restriction under the Listing Rules to prohibit an issuer from granting WVR to both corporate and individual beneficiaries (to the extent they are

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eligible), as this is a purely commercial matter between the shareholders and the issuer. (Question 27).

Our client has further observations and views on a number of questions set out in the Paper, which we set out below:

1. Minimum economic interests (Questions 3-6)

1.1. <u>*30% economic interests in the listing applicant at the time of listing*</u> – Our client would like to point out that the absence of a controlling shareholder (as defined under the Listing Rules) is not uncommon for Innovative Companies, as it is likely that they would have completed several rounds of fund raising before IPO and have a relatively diverse shareholding structure. This may be illustrated by the fact that, for WVR listed issuers or previous WVR listing applicants (including Xiaomi, Meituan, Bitmain and Zhaogang.com), none of their institutional shareholders (other than vehicles holding shares for the respective individual WVR beneficiaries) had an economic interests over 30% at the time of listing.

1.2. If potential corporate WVR beneficiaries are required to increase their economic interests to at least 30% notwithstanding the more commonly seen shareholding levels among Innovative Companies in the market as mentioned above, Hong Kong may be considered as a less welcome listing venue. Further, a requirement to increase the stake to 30% could necessitate a fundamental change of shareholding structure and cause a material impact to the listing applicant's ownership continuity. This would be prejudicial to both the listing applicant and its shareholders as this may delay the IPO timetable. If the economic interests of the potential corporate WVR beneficiary are required to be increased, the additional investment costs and the related risks (in particular timing risk), coupled with the relatively short 10-year sunset period being proposed could also outweigh the benefit of having any weighted voting rights (especially if the maximum voting per share is limited to five times only).

1.3. Our client proposes that the requirements for "*holding an economic interest of 30% (or a lower threshold as finally determined by the SEHK) and being the single largest shareholder*" should be revised, so that the corporate WVR beneficiary "***<u>either</u>*** *holds an economic interest of 30% (or a lower threshold as finally determined by the SEHK)* ***<u>or</u>*** *is the single largest shareholder at the time of listing*". These suggestions are in line with SEHK's principles that the corporate WVR beneficiary is sufficiently 'interested' in the listing applicant while also preserves the original shareholding structure of the listing applicant. Our client also suggests the SEHK to explore lowering the minimum economic interests threshold to 20%.

1.4. *Not less than 10% economic interests and have been materially involved in the management or the business of the listing applicant for at least the two financial years immediately prior to the listing applications* – Our client would also like to point out that, in general practice, investors with 10-30% economic interests would not normally be materially involved in the management of the listing applicant, but it is more often the case that these pre-IPO investors would have directors nomination rights.

1.5. Therefore, our client invites the SEHK to elaborate further on the requirement of "having been materially involved in the management or the business of the listing applicant" and consider whether "having a representative on the board of the listing applicant" is sufficient to satisfy such requirement.

1.6. *Compliance with guidance letter GL85-16* – Further, our client would like to invite the SEHK to consider creating an exception under guidance letter GL85-16 to allow a proposed corporate WVR beneficiary to subscribe for shares at the IPO. Currently, GL85-16 mandates that an existing shareholder with less than 5% voting rights (and no other special rights) before listing can subscribe for shares at an IPO. From our experience, the SEHK would not grant any waivers for shareholders who hold more than 5% or any connected persons to allow them to subscribe for IPO shares, which would hinder any potential corporate WVR beneficiary to subscribe for shares at the IPO for the purpose of meeting the minimum economic interests threshold.

1.7. *Maintaining 30% economic interests post listing* – If the SEHK accepts our client's proposals set out in paragraph 1.3 above, this requirement should also be changed correspondingly, to either maintaining at least 30% economic interest in the issuer, or maintaining the corporate WVR beneficiary's position as the single largest shareholder of the issuer on an ongoing basis. It is also suggested that, a grace period should be given to the corporate WVR beneficiary to remedy the situation (through purchase from secondary market or share issuance by the issuer to the corporate WVR beneficiary) in the event that it ceases to be the single largest shareholder (due to another shareholder's increase in holding and exceeding its level of holding in the issuer's shares). Our client suggests that, similar to the suggestion in paragraph 174(a) of the Paper, the WVR will only lapse if the corporate WVR beneficiary no longer has at least 30% economic interest in the issuer or no longer is the single largest shareholder for a continuous period of 30 days, ***and*** the issuer does not announce the relevant share issuance plan or any other proposal for increase of the corporate WVR beneficiary's shareholding, (this should also be included as an exception from requiring share issues on a non-pre-emptive basis without shareholder approval), within 30 days of the corporate WVR beneficiary first becoming not interested in at least 30% economic interests in the issuer or not the single largest shareholder.

1.8. <u>*Exception to issue shares on a non-pre-emptive basis to corporate WVR beneficiary without shareholders' approval*</u> – Our client suggests that conditions (c) and (d) in paragraph 144 of the Paper should adopt only one objective benchmark, namely the average trading price of the issuer, when determining whether the subscription is on the same or better terms as the original issuance that triggered the need for the subscription, and whether the subscription price is fair and reasonable. It may be difficult and impracticable to require the issuer to justify how the corporate WVR beneficiary's subscription and the original issuance (which could be as consideration shares for an acquisition) are otherwise on the same or better terms when the original issuance was in consideration of injection of certain assets or businesses.

1.9. Further, as submitted in paragraph 1.7 above, the exception from non-pre-emptive issuance should not limit to a follow on subscription only, but should also include all situations that lead to the corporate WVR beneficiary involuntarily becoming not interested in at least 30% economic interests in the issuer or not the single largest shareholder.

2. Maximum votes per share (Question 7)

2.1. Our client finds the current rationale for the difference in the maximum ratio of voting rights between individual WVR beneficiary and corporate WVR beneficiary not convincing to differentiate the two. Our client invites the SEHK to provide further justification and clarify the policy rationale for the difference.

2.2. Our client also invites the SEHK to allow corporate WVR beneficiary to have the same maximum ratio of weighted votes so that the listing applicant can have better flexibility to arrange different ratios between individual WVR beneficiaries and corporate WVR beneficiaries, which should be a commercial matter between the listing applicant and its shareholders.

3. Contribution by the corporate WVR beneficiary (Questions 8-12)

3.1. Our client agrees in principle that the corporate WVR beneficiary should provide contribution to the listing applicant, which is of a nature that cannot be easily replicated or substituted. However, condition (d) in paragraph 156 of the Paper (i.e. the condition that the core components within the ecosystem, and the listing applicant, are in substance being controlled by the corporate WVR beneficiary) creates a characteristic which is rather narrowly and unclearly defined. Our client invites SEHK to further substantiate the thinking behind that condition, or modify/delete that condition altogether.

3.2. Further, if the SEHK accepts our client's suggestion to lower the minimum economic interest that a corporate WVR beneficiary is required to maintain in the listing applicant, then the condition for having the listing applicant to be "in substance controlled by the corporate WVR beneficiary" may be contrary to the relevant ownership continuity and control analysis for the listing applicant.

4. Corporate representatives (Questions 20-21)

4.1. While the requirement to appoint a "Corporate Representative" to the listing applicant is acceptable in principle to our client, and generally in line with the right of a >30% investor as a shareholder, our client suggests that the definition of "Corporate Representative" should be broadened to include director, manager or secretary of, or any other person involved in the management of the relevant segment/ business or the relevant subsidiary of, the listing applicant.

4.2. The SFO defines "an officer" as a director, manager or secretary of, or any other person involved in the management of a company – applying that to an Eligible Entity, that would reasonably be interpreted as the board of directors and other senior management as disclosed in its public filings (e.g. annual reports). However, given the Eligible Entity is likely a conglomerate of different business units/segments with a large number of subsidiaries and entities operating across different localities and jurisdictions, it may not always be practicable to require a member of the management from such senior level of the Eligible Entity to serve as a director of the listing applicant. In particular, (a) it would create onerous commitment to require the "officer" of the Eligible Entity to serve in both companies, and may not be in the best interests of the shareholders of the Eligible Entity (or the best interest of the listing applicant); (b) the "officer" of the Eligible Entity may not necessarily be the best person who possesses the industry knowledge/experience to serve on the board of the listing applicant; and (c) appointing a representative from such senior level is not in line with general market practice.

5. Sunset (Questions 25-26)

5.1. Our client recognises that corporate life and human life are not comparable and understands the decision to provide for a sunset clause for the corporate WVR. However, a time-defined sunset clause is not ideal to address the issue and our client invites the SEHK to consider whether a time-defined sunset is necessary or if there are alternatives – taking into account that, the continuous commitment of the corporate WVR beneficiary's intangible contribution to the WVR issuer and the Corporate Representative will also dictate the existence of the WVR attached to the shares. Our client considers that the current event-based sunsets (including the ongoing requirements of (1) minimum economic interests; (2) Corporate Representative; and (3) access to the qualifying ecosystem) have provided sufficient and comparable safeguard as those for individual WVR beneficiary.

5.2. In the event that there are no alternatives to a time-defined sunset, our client suggests the 10-year sunset period should be extended to 20 years (especially if the minimum economic interests requirement remains at 30%), since an individual WVR beneficiary would normally be able to exercise his/her WVR rights for more than 10 years.

Our client believes the SEHK will work with market participants, including potential corporate WVR beneficiaries and the respective listing applicants, to design a set of rules that protects the public shareholders as well as reflects the market reality and needs of the relevant stakeholders, while enhances the development of Hong Kong as a preferred listing venue for Innovative Companies.

Yours sincerely

[redacted]

Clifford Chance